

COUNCIL/ADMINISTRATIVE POLICY

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1. CAPITAL FINANCING AND DEBT MANAGEMENT

1.1 Capital Financing

- 1.1.1 The City will consider the use of debt financing only for one-time capital improvement projects and only under the following circumstances.
 - 1.1.1.1 When the project's useful life will exceed the term of the financing.
 - 1.1.1.2 When project revenues or specific resources will be sufficient to service the long-term debt.
- 1.1.2 Debt financing will not be considered appropriate for any recurring purpose such as current operating and maintenance expenditures. The issuance of short-term instruments such as revenue, tax, or bond anticipation notes is excluded from this limitation. (See Council/Administrative Policy No. 10-4, Investment Policy).
- 1.1.3 Capital improvements will be financed primarily through user fees, service charges, assessments, special taxes, or developer agreements when benefits can be specifically attributed to users of the facility. Accordingly, development impact fees should be created and implemented at levels sufficient to ensure that new development pays its fair share of the cost of constructing necessary community facilities and infrastructure.
- 1.1.4 The City will use the following criteria to evaluate pay-as-you-go versus long-term financing in funding capital improvements:
 - 1.1.4.1 Factors Favoring Pay-As-You Go Financing:
 - 1.1.4.1.1 Current revenues and adequate fund balances are available or project phasing can be accomplished.
 - 1.1.4.1.2 Existing debt levels adversely affect the City's credit rating.
 - 1.1.4.1.3 Market conditions are unstable or present difficulties in marketing.
 - 1.1.4.2 Factors Favoring Long Term Financing:
 - 1.1.4.2.1 Revenues available for debt service are deemed to be sufficient and reliable so that long-term

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financings can be marketed with investment grade credit ratings.

- 1.1.4.2.2 The project securing the financing is of the type which will support an investment grade credit rating or the bonds are a suitable no rated credit in the case of land secured financings.
- 1.1.4.2.3 Market conditions present favorable interest rates and demand for City financing.
- 1.1.4.2.4 A project is mandated by state or federal requirements, and resources are insufficient or unavailable.
- 1.1.4.2.5 The project is immediately required to meet or relieve capacity needs and current resources are insufficient or unavailable.

1.2. **Debt Management**

- 1.2.1 The City will not obligate the General Fund to secure long-term financings except when marketability can be significantly enhanced.
- 1.2.2 An internal feasibility analysis will be prepared for each long-term financing which analyzes the impact on current and future budgets for debt service and operations. This analysis will also address the reliability of revenues to support debt service.
- 1.2.3 The City will conduct financings on a competitive basis for revenue and general fund debt obligations. Negotiated financings will be used when there is market volatility, the bonds are non-rated, or the financing entails the use of complex security or structure.
- 1.2.4 The City will seek a rating on any direct debt and will seek credit enhancements such as letters of credit or bond insurance when it will improve marketing and is cost effective.
- 1.2.5 The City will monitor all forms of debt annually coincident with the City's Financial Plan preparation and review process and report concerns and remedies, if needed, to the Council.
- 1.2.6 The City will diligently monitor its compliance with bond covenants and ensure its adherence to federal arbitrage regulations.

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- 1.2.7 The City will maintain good, ongoing communications with bond rating agencies about its financial condition. The City will follow a policy of full disclosure on every financial report and bond prospectus (Official Statement).
- 1.2.8 The City will use debt proceeds as a funding source for City Council approved one-time capital improvement projects.
- 1.2.9 Pursuant to Government Code Section 5852.1 "SB 450", for all new obligations issued after January 1, 2018, City Council or Authority reports, either in the Resolution or the staff report, must contain good faith estimates with respect to the obligation. Such good faith estimates may be provided to the City or the Authority by the Municipal Advisor, underwriter or placement agent. Each estimate should be based on the financing plan and current market conditions, including the proposed interest rate prevailing at the time of preparation of the estimate.
- 1.2.10 The City may issue the following types of debt: General Obligation Bonds, Certificates of Participation, Lease Revenue Bonds, Assessment Bonds, Special Tax Bonds, Water and Sewer Revenue Bonds or Installment Purchase/Installment Sale Agreements, Variable Rate Demand Obligations, Commercial Paper, Tax Revenue Anticipation Notes, Bond Anticipation Notes, Capital Leases or any other type of debt permitted under State or Federal law for local agencies.
- 1.2.11 **Variable Rate Debt**
- 1.2.11.1 To maintain a predictable debt service burden, the City may give preference to debt that carries a fixed interest rate. However, the City may consider variable rate debt in certain instances, such as:
- 1.2.11.1.1 **High Interest Rate Environment** - Current interest rates are above historic average trends.
- 1.2.11.1.2 **Variable Revenue Stream** - The revenue stream for repayment is variable, and is anticipated to move in the same direction as market-generated variable interest rates, or the dedication of revenues allows capacity for variability.
- 1.2.11.1.3 **Adequate Safeguards Against Risk** - Financing structure and budgetary safeguards are in place to prevent adverse impacts from interest rate shifts; such structures could include, but are not limited to,

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interest rate swaps, interest rate caps and the matching of assets and liabilities.

1.2.11.1.4 **Variable Rate Debt Capacity** - Consistent with rating agency guidelines, the percentage of variable rate debt outstanding shall not exceed 20% of the City's total outstanding debt (excluding land-secured debt).

1.2.12 **Interest Rate Risk Mitigation Policy (Swap Policy)**

1.2.12.1 An interest rate swap is an agreement between two parties to exchange one stream of interest payments for another, over a set period of time. Swaps are derivative contracts and trade over-the-counter. Investment and commercial banks with strong credit ratings are swap market-makers, offering both fixed and floating-rate cash flows to their clients. By convention, each participant in a swap transaction is known by its relation to the fixed rate stream of payments. The party that elects to receive a fixed rate and pay floating is the "receiver" and the party that received floating in exchange for fixed is the "payer." Both the receiver and payer are known as counterparties in the swap transaction.

1.2.12.2 The City is not considered an active issuer and therefore it is not appropriate for the City to enter into any interest rate swap agreements unless specifically approved by City Council action.

1.2.13 **Post Debt Issuance Tax Compliance Procedures for Tax-Exempt and Direct Pay Subsidy Bonds**

1.2.13.1 The purpose of these Post-Issuance Tax Compliance Procedures is to establish policies and procedures in connection with tax-exempt bonds and direct pay subsidy bonds (e.g. "build America bonds" or similar programs) ("Bonds") issued by or on behalf of the Brentwood Infrastructure Financing Authority (the "Authority") or the City of Brentwood (the "City" and, collectively with the Authority, the "Issuer") so as to ensure that the Issuer complies with all applicable post-issuance requirements of federal income tax law needed to preserve the tax-exempt or direct pay subsidy status of the Bonds.

1.2.13.2 Ultimate responsibility for all matters relating to Issuer financings and refinancing rests with the Treasurer/Controller of

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the Authority and the Director of Finance and Information Systems of the City (collectively, the “Responsible Officer”).

1.2.13.3 **External Advisors and Documentation**

1.2.13.3.1 The Responsible Officer and other appropriate Issuer personnel shall consult with bond counsel and other legal counsel and advisors, as needed, throughout the Bond issuance process to identify requirements and to establish procedures necessary or appropriate so that the Bonds will continue to qualify for the appropriate tax status. Those requirements and procedures shall be documented via Issuer resolutions(s), Tax Certificate(s) and/or other documents finalized at or before issuance of the Bonds. Those requirements and procedures shall include future compliance with applicable arbitrage rebate requirements and all other applicable post-issuance requirements of federal tax law throughout (and in some cases beyond) the term of the Bonds.

1.2.13.3.2 The Responsible Officer and other appropriate Issuer personnel also shall consult with bond counsel and other legal counsel and advisors, as needed, following issuance of the Bonds to ensure that all applicable post-issuance requirements in fact are met. This shall include, without limitation, consultation in connection with future contracts with respect to the use of Bond-financed assets and future contracts with respect to the use of output or throughput of Bond-financed assets.

1.2.13.3.3 The Responsible Officer and other appropriate Issuer personnel shall maintain compliance with the regulations set forth in Government Code Section 8855 (i), Rule 15(c)2-12 – Securities and Exchange Commission Rule 15(c)2-12, Continuing Disclosure and 8855(k) of the California Government Code (CDIAC Reporting).

The City shall remain in compliance with Rule 15c2-12, promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, by filing (to the extent required by the applicable continuing disclosure undertaking) its annual financial statements and other financial and operating data for the benefit of its bondholders within nine months of the close of the fiscal year, or by such other annual deadline required in any continuing disclosure agreement or certificate for any debt issue. The City shall maintain a log or file evidencing that all continuing disclosure filings have been made promptly.

A copy of all debt-related records shall be retained at the City’s

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offices. At minimum, these records shall include all official statements, bond legal documents/transcripts, resolutions, trustee statements, leases, and title reports for each City financing (to the extent available). Such records shall be retained while any bonds of an issue are outstanding and during the three-year period following the final maturity or redemption of the bond issue or, if later, while any bonds that refund bonds of that original issue are outstanding and for the three year period following the final maturity or redemption date of the latest refunding bond issue.

- 1.2.13.3.4 One of the City’s priorities in the management of debt is to assure that the proceeds of the debt will be directed to the intended use for which the debt has been issued. In furtherance of this priority, the following procedures shall apply:

The Responsible Officer shall retain, for the applicable period a copy of each annual report filed with the California Debt and Investment Advisory Commission (“CDIAC”) pursuant to Section 8855(k) of the California Government Code concerning (1) debt authorized during the applicable reporting period (whether issued or not), (2) debt outstanding during the reporting period, and (3) the use during the reporting period of proceeds of issued debt.

In connection with the preparation of each annual report to be filed with CDIAC pursuant to Section 8855(k) of the California Government Code, the Responsible Officer shall keep a record of the original intended use for which the debt has been issued, and indicate whether the proceeds spent during the applicable one-year reporting period for such annual report comport with the intended use (at the time of original issuance or as modified pursuant to the following sentence).

If a change in intended use has been authorized subsequent to the original issuance of the debt, the Finance Division shall indicate in the record when the change in use was authorized and whether the City Council, City Manager, or another City official has authorized the change in intended use. The Responsible Officer or designee shall report apparent deviations from the intended use in debt proceeds to the City Manager for further discussion, and if the City Manager determines appropriate in consultation with legal counsel (which may be bond counsel, if applicable, or the City Attorney), to the City Council.

1.2.13.4 **Role of the Issuer as Bond Issuer**

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- 1.2.13.4.1 Unless otherwise provided by Issuer resolutions, unexpended Bond proceeds shall be held by the Issuer, and the investment of Bond proceeds shall be managed by the Responsible Officer. The Responsible Officer shall maintain records and shall prepare regular, periodic statements to the Issuer regarding the investments and transactions involving Bond proceeds.
- 1.2.13.4.2 If an Issuer resolution provides for Bond proceeds to be administered by a trustee, the trustee shall provide regular, periodic (monthly) statements regarding the investments and transactions involving Bond proceeds.
- 1.2.13.5 **Arbitrage Rebate and Yield Requirements** (Unless a Tax Certificate documents that bond counsel has advised that arbitrage rebate will not be applicable to an issue of Bonds.)
The use of bond proceeds and their investments must be monitored to ensure compliance with all arbitrage rebate requirements of the Internal Revenue Code and related Internal Revenue Service regulations, in keeping with the covenants of the City and/or related entity in the tax certificate for any federally tax-exempt financing. The Responsible Officer shall ensure that all bond proceeds and investments are tracked in a manner which facilitates accurate calculation; and, if a rebate payment is due, such payment is made in a timely manner.
- 1.2.13.5.1 The Issuer shall engage the services of a Rebate Service Provider, and the Issuer or the Bond trustee shall deliver periodic statements concerning the investment of Bond proceeds to the Rebate Service Provider on a prompt basis.
- 1.2.13.5.2 Upon request, the Responsible Officer and other appropriate Issuer personnel shall provide to the Rebate Service Provider additional documents and information reasonably requested by the Rebate Service Provider.
- 1.2.13.5.3 The Responsible Officer and other appropriate Issuer personnel shall monitor efforts of the Rebate Service Provider and assure payment of required rebate amounts, if any, no later than 60 days after each 5-year anniversary of the issue date of the Bonds, and no later than 60 days after the last Bond of each issue is redeemed.
- 1.2.13.5.4 During the construction period of each capital project financed in whole or in part by Bonds, the Responsible Officer and other

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appropriate Issuer personnel shall monitor the investment and expenditure of Bond proceeds and shall consult with the Rebate Service Provider to determine compliance with any applicable exceptions from the arbitrage rebate requirements during each 6-month spending period up to 6 months, 18 months or 24 month, as applicable, following the issue date of the Bonds.

- 1.2.13.5.5 The Issuer shall retain copies of all arbitrage reports and trustee statements as described below under "Record Keeping Requirements".
- 1.2.13.6 **Use of Bond Proceeds** The Responsible Officer and other appropriate Issuer personnel shall:
 - 1.2.13.6.1 Monitor the use of Bond proceeds, the use of Bond-financed assets (e.g., facilities, furnishings or equipment) and the use of output or throughput of Bond-financed assets throughout the term of the Bonds (and in some cases beyond the term of the Bonds) to ensure compliance with covenants and restrictions set forth in applicable Issuer resolutions and Tax Certificates.
 - 1.2.13.6.2 Maintain records identifying the assets or portion of assets that are financed or refinanced with proceeds of each issue of Bonds.
 - 1.2.13.6.3 Consult with Bond Counsel and other professional expert advisers in the review of any contracts or arrangements involving use of Bond-financed facilities to ensure compliance with all covenants and restrictions set forth in applicable Issuer resolutions and Tax Certificates.
 - 1.2.13.6.4 Maintain records for any contracts or arrangements involving the use of Bond-financed facilities as might be necessary or appropriate to document compliance with all covenants and restrictions set forth in applicable Issuer resolutions and Tax Certificates.
 - 1.2.13.6.5 Meet at least annually with personnel responsible for Bond-financed assets to identify and discuss any existing or planned use of Bond-financed, assets or output or throughput of Bond-financed assets, to ensure that those uses are consistent with all covenants and restrictions set forth in applicable Issuer resolutions and Tax Certificates.

If the debt has been issued to finance a capital project and the project timeline or scope of project has changed in a way that all

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or a portion of the debt proceeds cannot be expended on the original project, the Finance Director shall consult with the City Manager and legal counsel (which may be bond counsel, if applicable, or the City Attorney) as to available alternatives for the expenditure of the remaining debt proceeds (including prepayment of the debt).

1.2.13.7 **Record Keeping Requirements** Unless otherwise specified in applicable Issuer resolutions or Tax Certificates, the Issuer shall maintain the following documents for the term of each issue of Bonds (including refunding Bonds, if any) plus at least three years:

1.2.13.7.1 A copy of the Bond closing transcript(s) and other relevant documentation delivered to the Issuer at or in connection with closing of the issue of Bonds.

1.2.13.7.2 A copy of all material documents relating to capital expenditures financed or refinanced by Bond proceeds, including (without limitation) construction contracts, purchase orders, invoices, trustee requisitions and payment records, as well as documents relating to costs reimbursed with Bond proceeds and records identifying the assets or portion of assets that are financed or refinanced with Bond proceeds.

1.2.13.7.3 A copy of all contracts and arrangements involving private use of Bond-financed assets or for the private use of output or throughput of Bond-financed assets.

1.2.13.7.4 Copies of all records of investments, investment agreements, arbitrage reports and underlying documents, including trustee statements.

1.2.14 **Debt Capacity**

1.2.14.1 **General purpose debt capacity** The City will carefully monitor its levels of general purpose debt. Because our general purpose debt capacity is limited, it is important that the City only use general purpose debt financing for high-priority projects where the City cannot reasonably use other financing methods; funds borrowed for a project today are not available to fund other projects tomorrow; and funds committed for debt repayment today are not available to fund operations in the future.

1.2.14.2 **Enterprise Fund debt capacity** The City will set enterprise fund rates at levels needed to fully cover debt service requirements as well as operations, maintenance, administration and capital improvement costs. The ability to

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afford new debt for enterprise operations will be evaluated as an integral part of the City's rate review and setting process.

1.2.15 **Land-Based Financings**

- 1.2.15.1 **Public purpose** There will be a clearly articulated public purpose in forming an assessment or special tax district in financing public infrastructure improvements including why this form of financing is preferred over other funding options such as impact fees, reimbursement agreements or direct developer responsibility for improvements.

- 1.2.15.2 **Active role** Even though land-based financings may be a limited obligation of the City, we will play an active role in managing the district. This means that the City will select and retain the financing team, including the financial advisor, bond counsel, trustee, appraiser, disclosure counsel, assessment engineer, bond insurer, LOC provider and underwriter as necessary. Any costs incurred by the City in retaining these services will be the responsibility of the property owners or developer, and will be advanced via a deposit or will be paid on a contingency fee basis from the proceeds from the bonds.

- 1.2.15.3 **Credit quality** When a district is requested by a developer, the City will carefully evaluate the applicant's financial plan and ability to carry the project, including the payment of assessments and special taxes during build-out. This may include detailed background, credit and lender checks, and the preparation of independent appraisal reports and market absorption studies.

- 1.2.15.4 **Reserve fund** A reserve fund should be established in the lesser amount of: the maximum annual debt service; 125% of the annual average debt service; or 10% of the bond proceeds.

- 1.2.15.5 **Value-to-debt-ratios** The minimum value of the property in the district, within the public improvements, should be at least three times the amount of the assessment or special tax debt.

- 1.2.15.6 **Capitalized interest during construction** Decisions to capitalize interest will be made on a case-by-case basis, with the intent to fund interest in cases where the payment cannot be posted to the tax roll for that tax year.

- 1.2.15.7 **Maximum burden** Annual assessments (or special taxes in the case of Mello-Roos or similar districts) should generally not exceed 1% of the sales price of the property; and total property taxes, special assessments and special tax payments collected on the tax roll should generally not exceed 2%.

- 1.2.15.8 **Benefit apportionment** Assessments and special taxes will be apportioned according to a formula that is clear, understandable, equitable and reasonably

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related to the benefit received by – or burden attributed to – each parcel with respect to its financed improvement.

- 1.2.15.9 **Special tax district administration** In the case of Mello-Roos or similar special tax districts, the total maximum annual tax should not exceed 110% of annual debt service. The rate and method of apportionment should include a back-up tax in the event of significant changes from the initial development plan, and should include procedures for prepayments.

- 12.15.10 **Foreclosure covenants** In administration of the district, the City shall structure foreclosure covenants in such a way as to insure the delinquency data is available from the county or the administrator prior to having to commence foreclosure proceedings.

- 1.2.15.11 **Disclosure to bondholders** In general, each property owner who accounts for more than 25% of the annual debt service or bonded indebtedness must provide ongoing disclosure information annually as described under SEC Rule 15(c)-12.

1.2.16 **Conduit Financings**

- 1.2.16.1 The City will consider requests for conduit financing on a case-by-case basis using the following criteria:
 - 1.2.16.1.1 The City's bond counsel will review the terms of the financing, and render an opinion that there will be no liability to the City in issuing the bonds on behalf of the applicant.
 - 1.2.16.1.2 There is a clearly articulated public purpose in providing the conduit financing.
 - 1.2.16.1.3 The applicant is capable of achieving this public purpose.

- 1.2.16.2 This means that the review of requests for conduit financing will generally be a two-step process: first asking the Council if they are interested in considering the request, and establishing the ground rules for evaluating it; and then returning with the results of this evaluation, and recommending approval of appropriate financing documents if warranted. This two-step approach ensures that the issues are clear for both the City and applicant, and that key policy questions are answered.

- 1.2.16.3 The work scope necessary to address these issues will vary from request to request, and will have to be determined on a case-by-case basis. Additionally, the City should generally be fully reimbursed for our costs in evaluating the request; however, this should also be determined on a case-by-case basis.

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1.2.17 **Refinancing Outstanding Debt**

1.2.17.1 The Responsible Officer shall have the responsibility to analyze outstanding bond issues for refunding opportunities that may be presented by underwriting and/or Municipal Advisor firms. The Responsible Officer will consider the following issues when analyzing possible refunding opportunities:

1.2.17.1.1 **Debt Service Savings** The City establishes a guideline net present value savings threshold goal of three percent (3%) of the refunded bond principal amount. The net present value savings will be net of all costs related to the refinancing. The City will evaluate each refunding candidate on a case-by-case basis. In evaluating such refundings and the appropriateness of a 3% or higher refunding goal, the City will take into account whether the refunding will be current or advance, and if the latter, the period of time before the call date and the efficiency of the refunding escrow.

1.2.17.1.2 **Restructuring** The City will refund debt when in its best interest to do so. Refunding will include restructuring to meet unanticipated revenue expectations, achieve cost savings, mitigate irregular debt service payments, release reserve funds, or remove unduly restrictive bond covenants.

1.2.17.1.3 **Term of Refunding Issues** The City may refund bonds within the term of the originally issued debt. However, the City may consider maturity extension, when necessary to achieve a desired outcome, provided that such extension is legally permissible. The City may also consider shortening the term of the originally issued debt to realize greater savings. The remaining useful life of the financed facility and the concept of inter-generational equity should guide this decision.

1.2.17.1.4 **Escrow Structuring** The City shall utilize the least costly securities available in structuring refunding escrows. The City will examine the viability of an economic versus legal defeasance on a net present value basis. In the case where open market securities are purchased, the City shall procure a minimum of three (3) competitive bids from approved broker-dealers. Such securities must be more cost effective than State and Local Government Obligations, and that the price paid for the securities must be reasonable within Federal guidelines. Under no circumstances shall the Underwriter or Municipal Advisor of a particular project sell escrow securities to the City from its own account.

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1.2.17.1.5 **Arbitrage** The City shall take all necessary steps to optimize escrows and to avoid negative arbitrage on any refunding.

1.3 **Financing Team Selection**

1.3.1 **Selection of Bond Counsel**

1.3.1.1 The issuance of debt by the City will include a written opinion by legal counsel affirming that the debt is a valid and binding obligation of the issuer of the debt and, to the extent the interest on the debt is expected to be excluded from gross income for federal income tax purposes, the exclusion of interest on the debt from gross income for federal income tax purposes. The approving opinion and other documents relating to the issuance of debt will be prepared by counsel with extensive experience in public finance and tax issues.

1.3.1.2 It is within the City's best interest to be in a position to be able to react quickly and issue debt based on favorable market conditions. Therefore, on a case-by-case basis, firms may be selected to work on a particular financing. The selection of Bond Counsel will be determined by the Responsible Officer in consultation with the City Attorney's Office.

1.3.1.3 Bond Counsel compensation shall be negotiated on a case-by-case basis.

1.3.2 **Selection of Disclosure Counsel**

1.3.2.1 In any sale of City debt in which legal counsel is required to represent the City, the Responsible Officer shall select a Disclosure Counsel from qualified firms in consultation with the City Attorney's office.

1.3.2.2 Disclosure Counsel compensation shall be negotiated on a case-by-case basis.

1.3.3 **Selection of Municipal Advisor**

1.3.3.1 The City may select a Municipal Advisor to assist in its debt issuance and debt administration processes. Selection of the City's Municipal Advisor(s) shall be based on, but not limited to, the following criteria:

- Experience in providing consulting services to complex issuers.
- Knowledge and experience in structuring and analyzing complex issues.
- Experience and reputation of assigned personnel.
- Fees and expenses.

1.3.3.2 Municipal Advisor compensation shall be negotiated on a case-by-case basis.