Comprehensive Debt Management Policy
Lexington-Fayette Urban County Government

I. INTRODUCTION

This debt management policy serves as a guide to the Lexington-Fayette Urban County Government (LFUCG) as to how it may issue debt, the types of acceptable debt it may issue, and the appropriate level of debt the municipal government may support.

II. SCOPE

The debt management policy of LFUCG applies to debt issued by LFUCG on behalf of the citizens, ratepayers, and taxpayers of LFUCG prior and subsequent to the creation of this document.

The debt management policy of LFUCG will:

(A) Establish guidelines regarding the purpose, type, structure, method of sale, usage, and maintenance of debt; and,

(B) Identify two metrics to evaluate the debt position of LFUCG.

III. OBJECTIVES

The comprehensive debt management policy of LFUCG contains eight objectives, each assisting LFUCG in the maintenance of its outstanding debt and management of future debt. The Commissioner of Finance will assume responsibility for the implementation and administration of this debt management policy.

A) CREDIT QUALITY

Credit Ratings
LFUCG seeks to maintain the highest possible rating for all categories of short-term and long-term debt that may be achieved without compromising the delivery of services and achievement of policy objectives. Granted, events external to LFUCG (i.e. economic conditions, natural disasters events, etc.) may affect the creditworthiness of the government's outstanding debt. However, aside from these external events, maintaining a favorable credit rating is a priority of this debt management policy.

Each proposal for additional debt will be analyzed to determine the sum of its impact upon the current credit rating of LFUCG. Projects found to possess volatile or risky debt repayment sources, which may adversely affect the credit rating of the governmental entity or public authority, will undergo further financial analysis by the Commissioner of Finance to determine the projects' eligibility for debt financing.

Relationships with Credit Rating Agencies

The Commissioner of Finance will be responsible for maintaining professional, working relationships with the credit rating agencies that assign ratings to the debt obligations of LFUCG. This effort includes providing periodic updates, both formal and informal, regarding the financial condition of LFUCG and planning and/or coordinating meetings and presentations in conjunction with new debt issuances. In addition, the Commissioner of Finance will determine, 1) Whether a rating will be requested for a specific debt issue, and 2) The credit rating agency, or agencies, responsible for providing the rating.

Long-Term Credit Rating Target

LFUCG desires to maintain a “double-A” credit rating for all direct, long-term, debt obligations.

Credit enhancements (Letters of Credit and Bond Insurance)

When found prudent and financially advantageous by the Commissioner of Finance, credit enhancements may be sought to improve the rating of the debt obligation if a debt obligation does not meet the required credit rating, based solely upon the credit strength of LFUCG. Debt obligations with a rating that might fall below the minimum requirement may be issued without a rating if the credit enhancement is unavailable or if the Commissioner of Finance determines that the cost of credit enhancement outweighs the monetary benefit of the credit enhancement on the sizing of the debt obligation. LFUCG may enter into an agreement with commercial banks or other financial institutions for purposes of acquiring letters of credit. These may be acquired to provide LFUCG with additional liquidity or to provide a credit enhancement to a specific debt issue. Prior to entering into any agreement, the Commissioner of Finance will plan for the acquisition of a letter of credit and must find such an agreement feasible and the Urban County Council of the LFUCG must approve of any agreement with any commercial bank or financial institution with the intent of acquiring letters of credit. In addition, LFUCG may use bond insurance to enhance a particular bond issue and provide a higher credit rating.

Financial Disclosure

LFUCG is committed to full and complete financial disclosure. LFUCG will fully comply with bond documents and will fully cooperate with rating agencies, departments and agencies of LFUCG, other levels of government, and the general public to disseminate clear, comprehensible and accurate financial information.

Specifically, LFUCG will disseminate economic and financial information to all Nationally Recognized Municipal Information Repositories (NRMSIRs) designated by the Securities and Exchange Commission (SEC) and to any State Information Depository (SID).

B) PURPOSES FOR ISSUING BOND DEBT

Purposes
Proceeds from bond sales may only be used to finance costs associated with the acquisition or construction of capital projects, including, but not limited to: Buildings, permanent structures, attached fixtures or equipment, planning and design, land acquisition and development, and equipment purchases—permanent or movable—whose life shall not depreciate before the maturity of the bond issue. Bond proceeds will not be used to fund operating expenses of day-to-day governmental activities nor will they be issued if the aggregate cost for projects to be financed fails to reach a total of $1,000,000. Prior to the issuance and sale of municipal securities, funding approval must be granted by the Urban County Council of the LFUCG.

C) TYPES OF DEBT PERMITTED AND CRITERIA FOR ISSUANCE

The type of instruments used by LFUCG to issue debt is subject to legal constraints, market conditions and availability, investor and consumer demand, and the nature of the project. LFUCG may issue any of the following long-term debt instruments:

General Obligation (GO) Bonds
General obligation (GO) bonds are secured by the full faith and credit of the LFUCG under the provisions of the Charter of LFUCG. These will be secured by the general fund revenues of LFUCG.

Revenue Bonds
Revenue bonds may be issued by LFUCG as long as the underlying capital project will create a sufficient stream of revenue to cover the debt service and eventual retirement of the principal amount of debt at the date of maturity.

Special Assessment/TIFs
Special Assessment Districts, designated geographic areas within LFUCG, are eligible for bond financing. Bonds issued for financing projects within a special assessment district will be repaid by a special assessment of the property within the designated area. Similar to revenue bonds, a financial analysis must indicate the underlying capital project will create a stream of

revenue sufficient to cover the required debt service and eventual retirement of the principal amount of debt at the date of maturity.

For short-to-intermediate term financing, LFUCG may issue bond anticipation notes (BANs), capital appreciation bonds (CABs), certificates of participation (COPs), tax anticipation notes (TANs), revenue anticipation notes (RANs), and capital leases. LFUCG may issue BANs, CABs, COPs, TANs, or RANs or enter into a capital lease agreement if found prudent and financially advantageous, following a comprehensive analysis by the Commissioner of Finance.

D) DEBT STRUCTURES

Term of Debt
In general, debt borrowed on behalf of LFUCG should be of a duration that does not exceed the useful life of the underlying capital project that it finances. LFUCG, to the fullest extent possible, should design the repayment of debt to expedite recapturing debt capacity for future use and match its cash flows to the anticipated debt service payments.

Backloading/Frontloading Debt Service
LFUCG will seek to structure debt with level principal and interest payments over the life of the debt. “Backloading/Frontloading” of debt service payments will be avoided except in instances where maturities serve to make overall debt service level or match a specific revenue stream.

Variable-Rate Debt
LFUCG prefers to issue fixed-rate bonds, but may issue variable-rate bonds, when appropriate, to realize lower borrowing-costs. Such a decision is typically driven by market conditions and will be thoroughly analyzed prior to the entrance of agreement. LFUCG will only issue variable-rate debt if found prudent and financially advantageous by the Commissioner of Finance. The percentage of net variable-rate debt outstanding (excluding debt which has been converted to synthetic fixed-rate debt and debt matched to assets) will not exceed 20% of LFUCG’s total outstanding debt and will take into consideration the amount and investment strategy of LFUCG’s operating cash.

Synthetic Debt
The use of synthetic debt instruments will be considered appropriate in the issuance or management of debt in instances where it has been demonstrated that the derivative product will either provide a hedge that reduces risk of fluctuations in expense or revenue, or alternatively, where it will reduce the total financing cost. The Commissioner of Finance will determine whether the use of derivatives and other synthetic debt

instruments is prudent, appropriate, and financially advantageous. Such an analysis will consider the risks and benefits associated with the use of a specific synthetic debt instrument. If upon approval of a synthetic debt instrument and the instrument requires a contract or written agreement with any third parties, such as letters of credit or swap agreements, LFUCG prefers to enter into contracts with financial institutions that have credit ratings equal to or higher than the credit of the underlying debt. Furthermore, if synthetic debt is recommended, the Commissioner of Finance will comply with any applicable state statutes and all federal regulations regarding the use of synthetic debt.

E) METHODS OF SALE

LFUCG prefers to issue debt through a competitive sale; however, LFUCG will determine the method of sale on a case-by-case basis. Debt issues are sold to an underwriter or underwriting syndicate through either competitive or negotiated bid sales. LFUCG will follow current procurement processes when issuing debt through either competitively bid or negotiated bid sales.

F) REFUNDING OF DEBT

Advance and Current Refundings
A refunding of bond issues with the intent to restructure current outstanding debt is an acceptable use of bond proceeds. LFUCG may issue an advance or current refunding when it is legally permissible, prudent, and financially advantageous, when a target of 3.00% net present value of the par amount of the refunding bond(s) is achievable.

Debt Restructuring
When bond covenants or other financial structures hinder LFUCG from exercising prudent and sound financial management, LFUCG may elect to refund outstanding debt. This refunding will not be held to the same cost-effective/savings standards as an advanced or current refunding and may be recommended by the Commissioner of Finance upon finding that such a restructuring is in LFUCG's overall best financial interest.

G) LEGAL DEBT LIMITS

Legal Limitations
LFUCG will abide by and comply with the legal debt limitation as proscribed by the Constitution of the Commonwealth of Kentucky, Section 158, which states:

> *Cities, towns, counties, and taxing districts shall not incur indebtedness to an amount exceeding the following maximum*

> *percentages on the value of taxable property therein, to be estimated by the last assessment previous to the incurring of the indebtedness: Cities having a population of fifteen thousand or more, ten percent (10%)...*

In addition to the debt limitations established by the Commonwealth of Kentucky, LFUCG will abide by and comply with debt service and debt limitation requirements set forth in the Charter of LFUCG, Section 8.11.

Non-Restrictive Debt
Long-term obligations that are payable from restricted sources are not subject to debt limitations. Examples of non-restrictive debt would include the financing or refinancing of projects from the issuance of debt instruments that are payable from restricted revenues or user fees, revenues generated from a project, special assessment districts, and taxes collected within a redevelopment project area/district in which the increased assessed valuation of the property within the area is a direct result of redevelopment as initiated and undertaken by LFUCG.

H) TESTS OF AFFORDABILITY AND CAPACITY

Affordability Targets – General Obligation Bond Debt
LFUCG will create and implement the following two ratios to evaluate its outstanding debt:

Evaluation Metric	**Target**
Debt Service as % of Operating Expenditures	10%
Debt Service as % of Recurring Revenue	10%

LFUCG will use these metrics to evaluate the affordability and its capacity to issue debt in the future. The metrics used by LFUCG to measure its affordability and capacity of issuing are defined as follows:

1) Debt Service as % of Operating Expenditures =

$$\frac{\text{Debt service expenditures for all General Operating Funds}}{\text{Operating Expenditures}}$$

2) Debt Service as % of Recurring Revenues =

$$\frac{\text{Debt service expenditures for all General Operating Funds}}{\text{Recurring Revenues}}$$

Operating expenditures are total expenditures for all general operating funds, including net transfers out. Recurring revenues are revenues earned LFUCG that do not reflect one-time tax initiatives (i.e. tax amnesty programs), temporary revenue sharing or revenue infusions by other governments, sale of surplus assets, and fund balance or Economic Contingency draws.

If these targets are not achieved, then LFUCG will work to create and implement a strategy toward achieving these financial targets.

Affordability Targets – Revenue Bond Debt
Generally, LFUCG will issue general obligation bonds as the primary long-term debt instrument. However, if determined financially and financially advantageous, LFUCG may issue self-supporting revenue bonds. In determining the affordability of proposed revenue bonds, LFUCG, by way of assistance from financial advisors, will perform an objective analysis that compares proposed annual revenues to the estimated annual debt service.