Debt Management
Standard Operating Procedure

October 19, 2018

College written procedure that states the authority to issue debt, what types of debt may be issued, structure of the debt, the process, and how debt will be managed. A glossary of terms is at the end of this Debt Management Standard Operating Procedure. The Governing Board's Finance and Audit Committee reviewed and approved this procedure on October 19, 2018.

Background

Debt management standard operating procedures (SOP) are written guidelines, allowances, and restrictions that guide the debt issuance practices of governments, including the issuance process, management of a debt portfolio, and adherence to various laws and regulations. A debt management procedure statement should improve the quality of decisions, articulate institutional goals, provide guidelines for the structure of debt issuance, and demonstrate a commitment to long-term capital and financial planning. Adherence to a debt management procedure signals to rating agencies and the capital markets that a government is well managed and therefore is likely to meet its debt obligations in a timely manner. Debt management procedures should be written with attention to the issuer's specific needs and available financing options and are typically implemented through more specific operating procedures.

I. Debt Limits and Other Legal Restrictions

A. *Authority and Legal Restrictions*

1. Arizona Revised Statutes

Title 15 Education, Chapter 12 Community Colleges; Title 35 Public Finances, Chapter 3 Public Indebtedness; Title 48 Special Taxing Districts, Chapter 3.

2. Debt Limits

(a) General Obligation Bonds and Financing Leases may not exceed 15% of the net limited property assessed valuation - Article 9, Section 8 of the Arizona Constitution.

(b) Revenue Bonds have no constitutional limitation but generally have more extensive bond covenants including additional bonds test, debt service coverage, and/or a reserve fund.

3. Municipal Securities Market

Securities and Exchange Act relating to the municipal securities market as promulgated by various rules of the Municipal Securities Rulemaking Board (MSRB).

4. Tax Exempt Bonds

Codes and regulations pertaining to the issuance and regulations of tax-exempt bonds as promulgated by various Internal Revenue Codes and Treasury Regulations.

B. *Public Policy*

1. Purpose of this Procedure

This procedure statement is intended to provide the controls, tools and framework by which decisions may be developed regarding the use and management of debt. Debt is generally used to acquire, build, improve and modify land, buildings and equipment that have a multi-year useful life.

2. Types of Debt the College May Issue

The College may issue all legally allowed debt instruments. The type of debt will be dependent on the size of the project, the type and useful life of the project, or the facility being acquired or built, as well as the state of the securities market. Each general type of debt has many different variations. The general types of debt include:

(a) General Obligation (GO) Bonds

The College may issue GO bonds for capital outlay, including the purchase of land, the purchase, construction, and remodeling of buildings, and the purchase of equipment and facilities for educational and auxiliary purposes. GO bonds are generally meant for large multiyear capital projects that require a large amount of funds. The bonds are usually secured by the full taxing authority of the College district. Generally, GO bonds are repaid through a secondary tax assessment on the net limited property assessed valuation, which serves as security for the bondholders. GO bonds are generally the least expense source of borrowing but most difficult to obtain because they require affirmative vote by the electorate. Further, the College is responsible for the election costs.

(b) Revenue Bonds
Revenue bonds carry a promise to repay from an identified revenue source or sources. The identified revenue generally serves as security for the bondholders.

(c) Certificates of Participation
An instrument evidencing a pro rata share in a specific pledged revenue stream, usually lease payments by the issuer that are subject to annual appropriation. The certificate generally entitles the holder to receive a share, or participation, in the lease payments from the particular project. The project being financed generally serves as the security for the certificate holders.

(d) Capitalized Lease
An agreement in which one party gains a long-term rental agreement and the other party receives a form of secured long-term debt; it meets certain tests of ownership such that the transaction is reflected as a capital asset for one party and a long-term liability for the other party.

(e) Pay-As-You-Go Financing
Except in extenuating circumstances, the College will fund routine maintenance projects in each year's capital program with pay-as-you-go financing. Extenuating circumstances may include unusually large and non-recurring budgeted expenditures, or when depleted reserves and weak revenues would require the delay or deletion of necessary capital projects.

3. Relationship to Capital Improvement Plan and other Processes

(a) Purchase, construction, or lease should always be for the furtherance of the mission, strategic plan, values, and vision of the College.
(b) Projects funded by this procedure statement should be integrated in the College's Capital Improvement Plan.
(c) Purchase, construction, or lease of land and buildings should be consistent with the Facilities Master Plan and relate to the Educational Master Plan.
(d) Purchase, construction, or lease of land and buildings may be considered outside the normal Capital Budgeting process.
(e) Purchase or lease of Equipment should generally be included with the Capital Budgeting process.

4. Goals and Objectives

(a) Use debt to finance mission critical projects to ensure that debt capacity is optimally used to fulfill the College's mission.
(b) Seek most available and cost effective source of financing that is needed to fund new projects and equipment with a multi-year useful life that will be used in the operations of the College.
(c) Limit the risk of the College's debt portfolio by applying risk mitigating procedures and mechanisms.
(d) Strive to maintain the College's credit ratings at the highest grade level possible.
(e) Monitor debt portfolio to seek opportunities to refinance or restructure current debt to lower interest cost.
(f) Comply with all debt agreements and indentures.

(g) Comply with all College policies as well as all state and federal laws, including any post-issuance compliance laws.
(h) Manage debt level to monitor that the College maintains and does not exceed adequate debt related financial ratios. For example, the College needs to maintain an adequate Viability Ratio, which is reported to Higher Learning Commission (HLC) in the annual update.
(i) Follow Debt Management best practices recommended by Government Finance Officers Association (GFOA).

II. Debt Structuring

A. Debt Service Structure

The College shall consider market conditions and College cash flows when timing the issuance of debt. The College shall design the financing schedule and repayment of debt so as to take best advantage of market conditions, provide flexibility, and, as practical, to recapture or maximize its debt capacity for future use. Annual debt service payments will generally be structured on a level basis per component financed; however, principal amortization may occur more quickly or slowly where permissible, to meet debt repayment, tax rate, and flexibility goals. Twenty years should generally be the maximum length on any financing issue.

B. Capitalized Interest

Unless required for structuring purposes, the College will avoid the use of capitalized interest in order to avoid unnecessarily increasing the bond size and interest expense. Certain types of financings may require that interest on the debt be paid from capitalized interest until the College has use and possession of the pledged asset. However, the College may pledge assets using an asset-transfer structure as collateral for the issue in order to eliminate the need for capitalized interest.

C. Call Provisions

The College, based upon analysis from the Financial Advisor of the economics of callable versus non-callable features, shall set forth call provisions for each issue.

D. Tax Exempt vs. Taxable

The College will generally seek to issue all of its debt financings on a tax-exempt interest rate basis, unless there is private use associated with the project or other need or benefit to be obtained from issuing taxable obligations. If there is private use, determination will be made of the extent of private use as defined in IRS Code Section 141 and, if such private use could exceed 10%, or the alternate 5% “disproportionate use” test, consideration will be given to using any available College funds for the private use and/or financing a portion of the project on a taxable interest rate basis.

E. Credit Enhancements

The College may enter into credit enhancement agreements such as municipal bond insurance, surety bonds, letters of credit, and lines of credit with commercial banks, municipal bond insurance companies, or other financial entities when their use is judged to lower borrowing costs, eliminate restrictive covenants, or have a net economic benefit to the financing. The College shall use a competitive process to select providers of such products to the extent applicable. To assure that the College uses credit enhancement cost-effectively, staff will review an economic analysis, by maturity where appropriate, prepared by the Financial Advisor before selecting which maturities to insure.

F. Intent to Reimburse

Before the start of project construction, a Declaration of Official Intent within the meaning of Treasury Regulations Section CFR 1.150-2 will, if necessary, be prepared and approved by a designated College representative, which generally will be the Chief Financial Officer

(CFO). The Declaration will permit the College to be reimbursed from the proceeds of a tax-exempt debt obligation for any College incurred expenditures that occurred prior to the issuance of the debt, subject to the Treasury Regulations.

G. *Use of Derivatives*

Derivative products may be considered where appropriate in the issuance or management of debt only in instances where it has been demonstrated through analyses that the derivative product will either provide a hedge which reduces risk of fluctuations in expense or revenue, or alternatively, where it will reduce total project cost. An analysis of early termination costs and other conditional terms will also be performed given certain financing and marketing assumptions. Such analyses will document the risks and benefits associated with the use of the particular derivative product. The College will retain a separate derivatives advisor, knowledgeable of such products. The College will issue a separate procedure statement and guidelines for use of derivatives that follows the GFOA advisory, "Use of Debt Related Derivatives Products and the Development of a Derivatives procedure statement".

III. Debt Issuance

Debt issuances are a major undertaking that require specialized skills. The College will need to assemble Consultants and internal team members to work on a debt issuance. Generally, the College may secure the services for Financial Advisor, Bond Counsel, Trustee/Paying Agent, and Underwriters in the usual procurement process. The College may also secure these services through procurements undertaken by the State of Arizona on behalf of all State agencies and political subdivisions.

A. Consultants and Financing Team Members

1. Financial Advisor

The College will select a Financial Advisor to assist in the debt issuance and debt administration processes, and will generally use a Financial Advisor on its debt financings. The Financial Advisor for a debt offering shall not also be an underwriter for the same debt offering. Selection of the College's Financial Advisor(s) should include the following criteria:

(a) Experience in providing consulting services to large and complex issuers;
(b) Knowledge and experience in structuring and analyzing complex debt financings and issues;
(c) Experience and reputation of assigned personnel; and
(d) Fees and expenses.

The Financial Advisor would provide services such as:

(a) Evaluation of risks and opportunities associated with debt issuance;
(b) Monitoring marketing opportunities;
(c) Evaluation of proposals submitted to the College by investment banking firms;
(d) Structuring and pricing of bond issues;
(e) Preparation of requests for procurement of other financial services (trustee and paying agent services, underwriting services, printing, credit facilities, remarketing agent services, etc.); and
(f) Providing advice, assistance, and preparation for presentations with rating agencies and investors.

2. Bond Counsel

College debt will include a written opinion by legal counsel affirming that:

(a) The College is authorized to issue the proposed debt and has met all constitutional and statutory requirements necessary for issuance, and
(b) A determination of the proposed debt's federal income tax status has been made.

The approving opinion and other documents relating to the issuance of debt will be prepared by a nationally recognized bond counsel firm counsel with extensive experience in public finance and tax issues.

3. Underwriters

   In selecting underwriters for most negotiated sales, the College will generally select several underwriters so that a syndicate of underwriters is formed for the transaction. In certain cases, such as smaller obligation financings, the College may select a single underwriter if it believes that to be in its best interests. There should be diversity among the firms selected so that most, if not all, financings are emphasized and covered for the various target markets and as desired by the College – e.g., institutional versus retail, or Arizona versus national distribution.

   Depending upon the financing, the College may also have each underwriter in the pool submit a short proposal for that specific financing that includes the firm's proposed marketing approach, personnel to be assigned, and underwriting costs. The underwriter(s) selected by the College for any financing will depend upon the size and complexity of the financing, timing issues, distribution capabilities, and other factors, with in most cases one of the underwriters designated by the College as the Senior Manager for the financing.

4. Disclosure Counsel

   The College will hire, when appropriate, Disclosure Counsel to prepare official statements in the event of a competitive sale. Disclosure Counsel will be responsible for ensuring that the official statement complies with all applicable rules, regulations, and guidelines. Disclosure Counsel should be a nationally recognized firm with extensive experience in public finance. Bond Counsel for a transaction may serve as Disclosure Counsel.

5. Pricing Consultant

   The College may engage the services of an independent pricing consultant, as needed, to evaluate the underwriters discount in a negotiated sale.

6. Bond Trustee

   The trustee is the authenticating agent, bond registrar, transfer agent, and paying agent for the College bond issues. The trustee will perform all duties outlined within the bond resolution or bond indenture in conjunction with all state and federal laws and regulations.

7. College Financing Team Members

   The CFO may select internal College team members to work with the consulting team members on debt financing projects. This may include the College General Counsel and other College employees as so determined by the CFO. Members of the Finance and Audit Committee may also be selected.

8. Disclosure by Financing Team Members.

   The College expects that all members of its financing team will at all times provide the College with objective advice and analysis, and be free from any conflicts of interest. All financing team members will be required to provide full and complete disclosure, under penalty of perjury, relative to any and all agreements with other financing team members and outside parties that could compromise any firm's ability to provide independent advice that is solely in the best interests of the College, or that could be perceived as a conflict of interest. The extent of disclosure may vary depending on the nature of the transaction.

B. *Sales Methods*

The College will generally utilize a sale process that seeks to obtain the lowest interest cost for the debt, using one of three possible methods of sale: competitive sale, negotiated sale, or private placement. As each type of sale has the potential to provide the lowest cost given the right conditions, a decision as to the type of sale will be determined based on market conditions and other factors at the time of sale.

1. Competitive Sale

May be used when Bond prices are stable and/or demand is strong.

2. Negotiated Sale

May be used when Bond prices are volatile and/or demand is weak or supply of competing bonds is high.

3. Private Placement

May be used for a small debt placement or refunding of debt. The College may privately place its securities with one or more sophisticated investors, if it is cost effective.

C. *Refunding*

The proceeds of a refunding bond are used to retire all or part of an outstanding prior bond issue. It is basically a refinancing of a debt. Refunding bonds may be issued to:

1. Take advantage of lower interest rates; the conversion from a high interest rate bond to a lower interest rate bond.
2. Restructure debt service - to defer or stretch out debt service obligations.
3. Remove old bond covenants that are too restrictive.

The College regularly monitors its existing debt for refinancing opportunities. Federal law places a number of complicated restrictions and requirements on the ability to issue tax-exempt debt to refinance existing tax-exempt debt. The College uses a case-by-case analysis to determine when to refinance debt.

While all these factors are considered on a case-by-case basis in evaluating debt of the College that may be refinanced, it is generally unlikely that a refinancing that saves less than 3% of the par amount of debt being refinanced, on a present value basis net of all issuance costs, would be undertaken. Generally, savings below this level are not economically sufficient to justify refinancing existing debt given federal tax law restrictions. In addition, the net present value savings must exceed any negative arbitrage associated with the refunding, subject to the CFO's discretion. The target net saving shall be no less than $1.0 million unless, at the discretion of the CFO, a lower amount is more appropriate given the nature of the particular escrow fund. Any savings from such restructuring shall be applied in accordance with legal and tax considerations and legal analysis at the time such savings are available.

D. *Credit Ratings*

The College, with a Financial Advisor if appropriate, will assess whether a credit rating should be obtained for an issuance. If it is determined that a credit rating is desirable, the probable rating of the proposed debt issuance is assessed before its issuance, and necessary steps are taken in structuring the debt issuance to ensure that the best possible rating is achieved. If a credit rating is used, one or more bond-rating firms (i.e., Standard and Poor's, Moody's Investors Service, or Fitch Ratings) will rate the College.

E. *Approval Process*

1. Governing Board Approval

All debt obligations require review and approval by the Governing Board prior to their issuance. In seeking approval, the College must disclose fully the estimated costs of the project and the debt issuance, information on debt capacity, outstanding debt levels, and debt service payments.

2. Legislative Review

Arizona statutes require a review of projects by the Joint Committee on Capital Review (JCCR) prior to the College undertaking a debt financing. For projects requiring JCCR review, the following generally applies:

(a) The Governing Board shall approve the projects prior to review by the JCCR.

(b) The projects shall receive a review from the JCCR prior to issuance of debt.

(c) Both the request for JCCR review and the request to the Board for debt issuance shall display full disclosure of the project description, estimated costs of the project, estimated bond issuance costs, and debt service funding sources.

(d) Use of project budget in excess of the amount initially approved by the Board and reviewed by the JCCR will require Board approval prior to seeking any additional review, if required, from the JCCR.

IV. Debt Management - Post Issuance

A. *Credit Objectives*

The College will actively seek to maintain and improve the credit ratings of its outstanding debt obligations.

B. *Investment of Bond Proceeds*

The College acknowledges its ongoing fiduciary responsibility to actively manage the proceeds of debt issued in a manner that is consistent with Arizona law and with the permitted securities covenants of related and executed bond documents. The College will comply with its Investment Standard Operating Procedure, which is reviewed annually by the Finance and Audit Committee. Where applicable, the College's official investment SOP and legal documents for a particular debt issuance shall govern specific methods of investment of bond related proceeds.

C. *Market Relationships*

1. Rating Agencies and Investors

   The College will maintain relationships with bond rating agencies, including Moody's Investors Service, Standard & Poor's, and/or Fitch Ratings and may:

   (a) Periodically meet with each of the College's credit analysts, and

   (b) Communicate with each of the College's analysts prior to each debt offering.

2. Continuing Disclosure

   It is the policy of the College to remain in compliance with the Security and Exchange Commission Rule 15c2-12 by filing its annual financial statements and other financial and operating data for the benefit of its underwriters and bondholders within seven months of the close of the fiscal year.

D. *Investor Community Relations*

The College shall endeavor to maintain a positive relationship with the investment community. The CFO, as necessary, shall prepare reports and other forms of communication regarding the College's indebtedness, as well as its future financing plans. This includes information presented to the media and other public sources of information. To the extent applicable, such communications shall be posted on the College's website.

E. *IRS Compliance and Record Keeping Requirements*

As most of the College's debt will be issued on a tax-exempt basis, there are requirements for compliance with various IRS Regulations, Revenue Procedures, and Revenue Rulings, based on consultations with bond counsel and bond tax counsel.

Glossary of Terms

ARBITRAGE

(1) With respect to the issuance of municipal securities, arbitrage usually refers to the difference between the interest paid on tax-exempt bonds and the interest earned by investing the proceeds of the tax-exempt bonds in higher-yielding taxable securities. Federal income tax laws generally restrict the ability to earn arbitrage in connection with tax-exempt bonds or other federally tax-advantaged bonds.

(2) Generally, transactions by which securities are bought and sold in different markets at the same time for the sake of the profit arising from a difference in prices in the two markets. *[Municipal Securities Rulemaking Board]*

ASSESSED PROPERTY VALUE

The Assessed Value is a percentage of the Full Cash Value and Limited Property Value. The Assessed Value of each property class is set by the Arizona Legislature in A.R.S. § 45-15001 and § 42-15010.

BONDS

When a government or other agency seeks to borrow funds to finance new infrastructure projects, cash flow needs, or refinance outstanding bonds, it often does so by issuing municipal bonds in the capital markets. This process usually involves municipal securities dealers or banks acting as underwriters or intermediaries between the issuer and investors. The underwriter agrees to purchase all of the bonds from an issuer and then resells those bonds to investors. There are many different types of investors in the municipal securities market, ranging from individuals, banks, insurance companies, trusts, mutual funds, hedge funds, and corporations, among others. *[Municipal Securities Rulemaking Board]*

Serial Bonds

In the municipal securities market, it is common for issuers to employ serial bonds to structure their debt. This financing technique involves the issuance of a number of different bonds that mature in consecutive years in one issue. Structuring the bonds in this way allows the issuer to repay principal over time and to make payments of principal that match revenue expectations over that time period. Although part of the same issue, each serial bond is a different security for purposes of sales and trading. *[Municipal Securities Rulemaking Board]*

Term Bonds

A bond with a single maturity that comprises the entire issue is sometimes called a term issue. If a large part of a serial bond issue is comprised of identical bonds with a single maturity date, the bonds with that maturity are called term bonds or a term maturity. In such issues, the term maturity normally will have a maturity date later than the last maturity of all of the serial bonds. *[Municipal Securities Rulemaking Board]*

CAPITALIZED INTEREST

A portion of the proceeds of an issue that is set aside to pay interest on the securities for a specified period of time. Interest is commonly capitalized for the construction period of a revenue-producing project, and sometimes for a period thereafter, so that debt service expense does not begin until the project is expected to be operational and producing revenues. Capitalized interest is sometimes referred to as “funded interest.” *[Municipal Securities Rulemaking Board]*

CERTIFICATE OF PARTICIPATION (COP)

An instrument evidencing a pro rata share in a specific pledged revenue stream, usually lease payments by the issuer that are typically subject to annual appropriation. The certificate generally entitles the holder to receive a share, or participation, in the payments from a particular project. The payments are passed through the lessor to the certificate holders. The lessor typically assigns the lease and the payments to a trustee, which then distributes the payments to the certificate holders. *[Municipal Securities Rulemaking Board]*

COMPETITIVE SALE

A method of sale chosen by an issuer, requesting underwriters to submit a firm offer to purchase a new issue of municipal securities. The issuer awards the municipal securities to the "winning" underwriter or syndicate presenting a bid complying with the terms of a Notice of Sale that provides the lowest interest rate cost according to stipulated criteria set forth in the Notice of Sale. The underwriting of securities in this manner is also referred to as a "public sale" or "competitive bid." *[Municipal Securities Rulemaking Board]*

DEBT SERVICE COVERAGE RATIO

The ratio of available revenues available annually to pay debt service over the annual debt service requirement. This ratio is one indication of the availability of revenues for payment of debt service. The formula for determining coverage, often referred to as "debt service coverage" or the "coverage ratio," is as follows:

EXAMPLE: $$\text{Coverage} = \frac{\text{Available Revenues}}{\text{Debt Service Requirement}}$$

$$\text{Coverage} = \frac{\$2{,}000{,}000}{\$1{,}200{,}000} = 1.66$$

[Municipal Securities Rulemaking Board]

DEBT SERVICE FUND

A fund into which the issuer makes periodic deposits to assure the timely availability of sufficient funds for the payment of debt service requirements. Typically, the amounts of the revenues to be deposited into the debt service fund and the timing of such deposits are structured to ensure a proper matching between debt service fund deposits and debt service payments becoming due. For many issues, the debt service fund may contain a separate "principal account" and "interest account" in which funds for such respective purposes are held. In addition, the debt service fund for many variable rate securities may contain a "letter of credit account," a "swap payments account" or "reimbursement account" in which funds are held to reimburse the issuer of a liquidity facility for draws made to pay amounts owing on the securities, or payments due under a swap agreement. *[Municipal Securities Rulemaking Board]*

DEBT SERVICE RESERVE FUND or RESERVE FUND

A fund in which funds are placed to be applied to pay debt service if pledged revenues are insufficient to satisfy the debt service requirements. The debt service reserve fund may be entirely funded with bond proceeds at the time of issuance, may be funded over time through the accumulation of pledged revenues, may be funded with a surety or other type of guaranty policy (described below), or may be funded only upon the occurrence of a specified event (e.g., upon failure to comply with a covenant in the bond contract) (a "springing reserve"). Issuers may sometimes authorize the provision of a surety bond or letter of credit to satisfy the debt service reserve fund requirement in lieu of cash. If the debt service reserve fund is used in whole or part to pay debt service, the issuer usually is required to replenish the fund from the first available revenues, or in periodic repayments over a specified period of time. *[Municipal Securities Rulemaking Board]*

GENERAL OBLIGATION BOND (GO BOND)

Typically refers to a bond issued by a state or local government that is payable from general funds of the issuer, although the precise source and priority of payment for general obligation bonds may vary considerably from issuer to issuer depending on applicable state or local law. Most general obligation bonds are said to entail the full faith and credit (and in many cases the taxing power) of the issuer, depending on applicable state or local law. General obligation bonds issued by local units of government often are payable from (and in some cases solely from) the issuer's ad valorem taxes, while general obligation bonds issued by states often are payable from appropriations made by the state legislature. *[Municipal Securities Rulemaking Board]*

GOVERNMENTAL FINANCE OFFICERS ASSOCIATION (GFOA)

The Government Finance Officers Association (GFOA), founded in 1906, represents public finance officials throughout the United States and Canada. The association's more than 19,000 members are federal, state/provincial, and local finance officials deeply involved in planning, financing, and implementing thousands of governmental operations in each of their jurisdictions. GFOA''s mission is to promote excellence in state and local government financial management. GFOA has accepted the leadership challenge of public finance. To meet the many needs of its members, the organization provides best practice guidance, consulting, networking opportunities, publications including books, e-books, and periodicals, recognition programs, research, and training opportunities for those in the profession. *[GFOA –www.gfoa/about-gfoa]*

LETTER OF CREDIT (LOC)

An irrevocable commitment, usually made by a commercial bank, to honor demands for payment of a debt upon compliance with conditions and/or the occurrence of certain events specified under the terms of the letter of credit and any associated reimbursement agreement. A letter of credit is frequently used to provide credit and liquidity support for variable rate demand obligations and other types of securities. Bank letters of credit are sometimes used as additional sources of security for issues of municipal notes, commercial paper or bonds, with the bank issuing the letter of credit committing to pay principal of and interest on the securities in the event that the issuer is unable to do so. *[Municipal Securities Rulemaking Board]*

MUNICIPAL SECURITIES RULEMAKING BOARD (MSRB)

The MSRB is a self-regulatory organization created under the Securities Acts Amendments of 1975. It is also incorporated as a Virginia non-stock corporation. The MSRB regulates the municipal securities market. MSRB mission is to protect investors, municipal entities and the public interest by promoting a fair and efficient municipal market, regulating firms that engage in municipal securities and advisory activities, and promoting market transparency. *[MSRB –www.msrb.org/About-MSRB.aspx]*

NEGATIVE ARBITRAGE

Investment of bond proceeds and other related funds at a rate below the bond yield. Negative arbitrage occurs when the escrow yields less than the arbitrage yield on the refunding bonds. The arbitrage yield is the amount that is “allowed” to be earned by investments in the escrow based on the average borrowing costs less costs of issuance. *[Municipal Securities Rulemaking Board]*

NEGOTIATED SALE

The sale of a new issue of municipal securities by an issuer directly to an underwriter or underwriting syndicate selected by the issuer. A negotiated sale is distinguished from a sale by competitive bid, which requires public bidding by the underwriters. Among the primary points of negotiation for an issuer are the interest rate, call features and purchase price of the issue. The sale of a new issue of securities in this manner is also known as a negotiated underwriting. *[Municipal Securities Rulemaking Board]*

NET LIMITED ASSESSED PROPERY VALUATION

The Limited Property Value is a statutory calculated value based on the Arizona Constitution and Statutes (see ASSESSED PROPERTY VALUE). Arizona's property tax system "classifies" property according to its usage. Each class of property is assigned an assessment ratio, pursuant to state law, ranging from 1% to 18% (currently). The assessment ratios are applied to both the Full Cash and Limited Values of a property and determine a property's "net assessed value.” All classifications within a taxing jurisdiction use the same tax rates.

The Limited Property Value may continue to rise annually but can never exceed the Full Cash Value. Beginning in tax year 2015, the tax rates are applied only to the Net Limited Assessed Property Value (primary value). *[Arizona Department of Revenue]*

NET PRESENT VALUE

The net present value is the difference between the present value of cash inflows and the present value of cash outflows over a period of time. For a refunding, this is the difference expressed in terms of current dollars between the debt service of the refunded bond debt service (prior debt) and the debt service on the refunding bond issue for an issuer. It is calculated by discounting the difference in the future debt service payments on the two issues at a given rate. *[Municipal Securities Rulemaking Board]*

PLEDGED REVENUES

The funds obligated for the payment of debt service and the making of other deposits required by the bond contract. Gross Pledge or Gross Revenue Pledge – A pledge that all revenues received will be used for debt service prior to deductions for any costs or expenses. Net Pledge or Net Revenue Pledge – A pledge that net revenues will be used for payment of debt service. *[Municipal Securities Rulemaking Board]*

PRICING ADVISOR

A consultant who provides a fairness letter to an issuer or its agent regarding the fairness of the pricing of a new issue of municipal securities. *[Municipal Securities Rulemaking Board]*

PRIVATE PLACEMENT

A primary offering in which a placement agent sells a new issue of municipal securities on behalf of the issuer directly to investors on an agency basis rather than by purchasing the securities from the issuer and reselling them to investors. Investors purchasing privately placed securities often are required to agree to restrictions as to resale and are sometimes requested or required to provide a private placement letter to that effect. *[Municipal Securities Rulemaking Board]*

REDEMPTION PROVISIONS

The terms of the bond contract, sometimes referred to as "call or prepayment provisions," giving the issuer the right to redeem or call (an "optional redemption"), or requiring the issuer to redeem or call (a "mandatory redemption"), all (an "in-whole redemption") or a portion (a "partial redemption") of an outstanding issue of bonds prior to its stated date of maturity. Bonds may be redeemed at a specified price, usually at par or accreted value in the case of original issue discount bonds or zero coupon bonds (a "par call") or above par or accreted value (a "premium call"), plus any accrued interest to the redemption date. Issuers may be limited to redeeming bonds on interest payment dates (an "any-interest-date redemption") or may be permitted to redeem bonds on any date (an "any time or continuous call").

Optional redemptions often can be exercised only on or after a specified date, typically for a municipal security beginning approximately ten years after the issue date. Some types of mandatory redemptions occur either on a scheduled basis (made in specified amounts or in amounts then on deposit in the sinking fund) or whenever a specified amount of money is available in the sinking fund ("sinking fund redemptions"). In addition, the occurrence of certain one-time or extraordinary events specified in the bond contract (an "extraordinary redemption") may trigger an optional (an "extraordinary optional redemption") or mandatory redemption (an "extraordinary mandatory redemption"). An extraordinary redemption may be triggered by, among other things, bond proceeds remaining unexpended by a specified date (an "unexpended proceeds redemption"), a determination that interest on the bonds is taxable (a "tax call"), a change in use of a project financed with bond proceeds that would cause interest on the bonds to become taxable (a "change in use call"), a failure of the issuer to appropriate funds needed to pay debt service on lease rental bonds or certificates of participation that are subject to appropriation (an "appropriation or non-appropriation call"), or the destruction of the facilities from which the bonds are payable (a "calamity or catastrophe call").

In a partial redemption of an issue, the maturities from which bonds will be redeemed (a) may be selected in maturity or inverse maturity order, or (b) may be made from all or selected maturities in a manner designed to maintain a desired debt service payment characteristic with respect to the bonds that remain outstanding (a "strip call"), or (c) may be selected in the discretion of the issuer or conduit borrower. Where a particular maturity of an issue is subject to partial redemption, the specific bonds to be redeemed may be selected by lot or (if the bonds are certificated) in numerical or inverse numerical order. *[Municipal Securities Rulemaking Board]*

REFUNDING

A procedure whereby an issuer refinances outstanding bonds by issuing new bonds. There are generally two major reasons for refunding: to reduce the issuer's interest costs or to remove a burdensome or restrictive covenant imposed by the terms of the bonds being refinanced. The proceeds of the new bonds are either deposited in escrow to pay the debt service on the outstanding bonds when due in an "advance refunding" or used to promptly (typically within 90 days) retire the outstanding bonds in a "current refunding." The new bonds are referred to as the "refunding bonds," and the outstanding bonds being refinanced are referred to as the "refunded bonds" or the "prior issue." Generally, refunded bonds are not considered a part of the issuer's debt because the lien of the holders of the refunded bonds, in the first instance, is on the escrowed funds, not on the originally pledged source of revenues. *[Municipal Securities Rulemaking Board]*

Current Refunding

A refunding transaction where the municipal securities being refunded will all mature or be redeemed within 90 days or less from the date of issuance of the refunding issue. Certain federal income tax rules relating to permitted yields of invested proceeds of the refunding issue, rebate of arbitrage earnings and the ability to refund certain types of municipal securities may be less restrictive in the case of current refundings as contrasted with advance refundings. *[Municipal Securities Rulemaking Board]*

Advance Refunding

For purposes of certain tax and securities laws and regulations, a refunding in which the refunded issue remains outstanding for a period of more than 90 days after the issuance of the refunding issue. Typically, such refunded bonds are secured solely by an escrow funded with the proceeds of the refunding bonds. The proceeds of the refunding issue are generally invested in Treasury securities or federal agency securities (although other instruments are sometimes used), with principal and interest from these investments being used (with limited exceptions) to pay principal and interest on the refunded issue. Bonds are “escrowed to maturity” when the proceeds of the refunding issue are deposited in an escrow account for investment in an amount sufficient to pay the principal of and interest on the issue being refunded on the original interest payment and maturity dates, although in some cases an issuer may expressly reserve its right (pursuant to certain procedures delineated by the SEC) to exercise an early call of bonds that have been escrowed to maturity. Bonds are considered “prerefunded” when the refunding issue’s proceeds are escrowed only until a call date or dates on the refunded issue, with the refunded issue redeemed at that time. The Internal Revenue Code and regulations thereunder restrict the yield that may be earned on investment of the proceeds of an advance refunding issue.

Refundings in which the refunded bonds are outstanding for less than 90 days are not advance refundings for federal tax purposes, but they may be advance refundings under state law or the provisions of bond contracts requiring specified comfort that the escrow securing payment of the refunded bonds is adequate. There are several methods of advance refunding or achieving the same practical effect as an advance refunding. *[Municipal Securities Rulemaking Board]*

REVENUE BOND

A bond that is payable from a specific source of revenue. Pledged revenues may be derived from operation of the financed project, grants, or excise or other specified non-ad-valorem taxes. Generally, no voter approval is required prior to issuance of such obligations. Only the revenue specified in the bond contract is required to be used for repayment of interest and principal. *[Municipal Securities Rulemaking Board]*

SURETY BOND

A third-party instrument that provides security against a default in payment. Surety bonds are sometimes used in lieu of a cash deposit in a debt service reserve fund. *[Municipal Securities Rulemaking Board]*

UNDERWRITING PROCESS

Municipal bonds typically are brought to market through an underwriting process. As part of this process, one or more municipal securities dealers – also known as underwriters – purchase newly issued securities from the issuer and sell the securities to investors. *[Municipal Securities Rulemaking Board]*

Assembling the Financing Team

Once a state or local government decides to finance a capital project by issuing bonds, it would hire a financing team to finalize the financing plan, develop offering documents, prepare for any rating agency and investor presentations, market the bond offering to investors, price the bonds and close the transaction. Generally, the bond offering process is a coordinated effort among various professionals, such as municipal advisors, bond counsel, underwriters, underwriter's counsel, rating agencies, trustees and others. Read more about the roles and responsibilities of the financing team in an initial municipal bond offering. *[Municipal Securities Rulemaking Board]*

Pricing the Security

The initial offering price is the price at which a new issue of municipal securities is offered to the public at the time of original issuance. In some cases, the initial offering price is set at a premium or discount to par value. Municipal bonds normally are sold to investors based on the yield of the transaction --an expression of annual rate of return on an investment -- and takes into account any premium or discount from the par value. For example, a transaction priced at 100% of par value of a bond will have a yield equal to the stated interest rate on the bond often referred to as the coupon, while a transaction priced at a discount to par value will have a yield higher than the coupon. *[Municipal Securities Rulemaking Board]*

The specific yields at which new issues are sold reflect a number of factors relating to the market value of the securities being offered. These include characteristics of the specific securities being offered – type of security, terms and features and credit quality, for example – as well as the general interest rate environment and credit market conditions. *[Municipal Securities Rulemaking Board]*

Underwriting Spread

The gross underwriting spread, which represents expenses and compensation to the underwriter distributing new issue securities to investors, is the difference between the price paid by investors and the amount paid by an underwriter to the issuer. For example, if the issuer issues $10,000,000 in bonds for sale to investors at an initial offering price of par (face value), and the underwriting spread is 1%, the issuer would receive $9,900,000. The exact amount received by an underwriter depends on whether the initial offering price was obtained for all of the securities in the issue. *[Municipal Securities Rulemaking Board]*