MECKLENBURG COUNTY
DEBT POLICY

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Introduction

The Debt Policy guides the issuance and repayment of debt in support of effective and efficient financial management. A debt policy establishes the parameters for issuing and managing debt. It also provides guidelines regarding the timing and purposes for which debt may be issued, the types of permissible debt, and the methods of sale that may be used.

MECKLENBURG COUNTY
DEBT POLICY

The Debt Policy is used in conjunction with the County's operating and capital budgets, Capital Improvement Program (CIP), and other financial policies. The Debt Policy:

- Enhances the quality of decisions;
- Documents the decision-making process;
- Identifies objectives for staff to implement;
- Demonstrates a commitment to long-term financial planning objectives; and
- Factors positively in private sector credit rating agencies' review of the County's credit policy.

The Debt Policy below reflects private sector credit rating agency guidance and criteria for highly-rated jurisdictions, the Local Government Commission (LGC) and best practices as outlined by the Government Finance Officers Association.

Long-Term Debt Instruments

General Obligation Bonds: General obligation ("GO") bonds are secured by a promise to levy taxes in an amount necessary to pay debt service—principal and interest due each fiscal year. General obligation bonds are backed by the full faith and credit of the County. These bonds are either authorized by a referendum, or through a non-voted (two-third's) authorization by the governing body. The authority for non-voted authorization allows governments to issue up to two-thirds of the previous year's net debt reduction without a referendum.

Revenue Bonds: Revenue bonds are repaid from pledged revenues generated by debt-financed asset, or by the operating system of which that asset is a part.

Special Obligation Bonds: Special obligation bonds are bonds that are payable from the pledge of revenues other than locally-levied taxes. Examples include beer and wine tax or enterprise revenues.

Installment Financing/Limited Obligation Bonds (LOB): These are alternative financing methods that do not require voter approval.

Installment financing can take several forms. An Installment Purchase Contract is an agreement in which equipment or property is acquired, and repaid over a period, with or without interest. This type of structure can be used to finance a wide-range of capital projects and equipment purchases.

Limited obligation bonds or certificates of participation are bonds that are issued to finance a project or asset. Revenues resulting from the operation or lease of the project are pledged to repay the debt.

Short-Term Debt Instruments

Generally, a government issues long-term debt based on when the bond proceeds are needed to begin construction on capital projects. However, other borrowing instruments may be more efficient and cost effective under specific circumstances. The County may consider short-term financing options, such as those outlined below, where such financing provides an efficient and effective means of financing. The County may consider other short-term or variable rate borrowing structures not listed below, including but not limited to, floating rate notes and variable rate demand bonds. The County will evaluate such options taking into account the projects being financed, the expected timing of cashflows and funding needs, the County's overall financial position, and current market conditions, among other factors.

Bond Anticipation Notes: Bond anticipation notes are short-term obligations issued in advance of a larger, future bond issue. In certain circumstances, it may be appropriate for the County to issue short-term obligations to provide interim or bridge financing for a project with the intention of refinancing the notes with long-term debt or retiring the notes with other funds.

Commercial Paper: Commercial Paper ("CP") is a short-term obligation with maturities ranging from 1 to 270 days. The County may consider utilizing CP as interim financing during the design and/or construction period to take advantage of typically lower interest rates at the short-term end of the yield curve. Once a capital project is completed, the County may recommend refunding CP with debt instruments.

Draw-Down Facility: A draw-down facility is a loan placed with a bank with a stated maximum balance and term, similar to a line of credit. As the County spends money on a capital project, the County would "draw" funds on the facility increasing the outstanding loan balance. The County would pay interest primarily on the "drawn" balance of the loan – not the maximum balance. This type of facility can be used to minimize initial interest costs prior to the project being completed.

Internal Financing

Another financing option the County may consider is internal financing, which is the use of internal sources (Pay-as-you-go "PAYGO") to finance capital improvement projects or other purchases in place of third-party financing, such as pay as you go ("PAYGO"). The County will evaluate the use of internal financing where it offers economic and/or

administrative efficiencies. Any internal financing structured as debt, such as a loan to the Solid Waste Enterprise Fund, will be repaid in full with interest and may not be forgiven except with the written authorization of the Director of Finance and the County Manager. All loans will be required to pay a rate of interest, which will be established by the Director of Finance and the County Manager at the time of execution.

Other Financing Options

The list above is not an exhaustive list of options available to the County. The County will evaluate other financing options, their legality under state statutes, and whether use of any such instrument would result in improved financing results for the County.

County Debt Policy

a. Debt shall not be used to finance ongoing operational expenses.

b. Any debt issued shall not have a maturity date beyond the useful life of the asset being acquired or constructed by the debt proceeds.

c. The County shall establish an affordable debt level to preserve credit quality and ensure sufficient revenue is available to pay annual debt service. This will be balanced against the County's need to maintain its infrastructure and manage growth.

d. The County will use appropriate debt instruments to provide funding for capital assets at the lowest cost with minimal risk. The County will monitor its debt positions to maintain the lowest effective cost.

e. The County will, at all times, manage its debt and sustain its strong financial position, including healthy reserves, to seek and maintain the highest credit rating possible.

f. The County will maintain a Debt Service Fund to provide dedicated funding and management of general debt issuances and expenditures.

g. The County shall utilize pay-as-you go and other alternative sources of funding for capital projects to minimize debt levels. To have an effective pay-as-you-go program, at least one funding source must be identified that is consistent, reliable, and large enough to provide for capital needs in an amount that reduces dependency on debt.

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Purposes for Debt Issuance

The County may issue debt to acquire or construct capital assets including land, buildings, machinery, equipment, technology, furniture, fixtures and any other eligible expenses specifically indicated in the Capital Improvement Policy. When feasible, debt issuance will be pooled together to minimize issuance expense. The County will prepare and adopt a Capital Improvement Program (CIP) to identify and establish an orderly plan to meet the County's infrastructure needs. The CIP will also identify all financing sources and the related debt service impact.

Debt Structure

Debt will be paid off in a timeframe that is less than or meets the useful life of the asset or project acquired through the financing. The life of the debt, interest mode, and principal maturity schedule make up the structure of the debt. This debt could be general obligation, revenue or special obligation bonds or limited obligation bonds or short-term instruments, or installment financing.

The County may consider various financing techniques, including fixed or variable interest rate debt, and interest rate swap agreements or derivatives to minimize costs and risk over the life of the issue. The County will review any such proposed structure with its financial advisors and legal counsel to determine if the use of any swap or derivative is appropriate and warranted given the potential benefit, costs, risks, and objectives. The County will evaluate the use of swaps or derivatives based on market conditions. The County will limit the issuance of variable rate debt to help maintain the County's "AAA" credit ratings. The County's long-term variable rate debt ratio limit is 15% of total outstanding debt. The County shall not pursue swaps, derivatives, variable rate debt, or other structures for speculation.

Debt Ratios

The County shall abide by the following debt ratios:

- Direct Debt as a Percentage of Assessed Valuation

  This ratio measures direct debt levels, debt issued by Mecklenburg County, against the property tax base which generates the tax revenues that are the main source of debt repayment. The ceiling for this ratio is 1.75%

- Direct Debt per Capita

  This ratio measures the burden of direct debt placed on the population supporting the debt. This measure will not exceed $2,000.

- General Debt Service as a percentage of Operational Expenditures

  This ratio reflects the County's budgetary flexibility to adapt spending levels and respond to economic condition changes. This ratio is targeted at a level of 17%.

- Ten-year Payout Ratio

  This ratio reflects the amortization of the County's outstanding debt. A faster payout is considered to be a positive credit attribute. The County will maintain a floor for its ten-year payout of 64.0%.

In addition, the County will monitor the following debt ratios, which are impacted by external partners and economic trends.

- Overall Debt as a Percentage of Assessed Valuation

  This ratio measures debt levels against the property tax base which generates the tax revenues that are the main source of debt repayment. The county will manage within a ceiling of 4.0% for this ratio.

- Overall Debt per Capita

  This ratio measures the burden of debt placed on the size of the population supporting the debt and includes debt issued by municipalities within the County. It is widely used by rating analysts as a measure of an issuers' ability to repay debt. This measure will not exceed $4,000.

These ratios will be calculated and reported each year in conjunction with the capital budget process, the annual financial audit and as needed for fiscal analysis. The county will also manage debt within parameters of related financial policies, including the General Fund Balance Policy.

Debt Management Policies

a. The County will issue debt only for purposes of constructing or acquiring capital assets and for making major renovations to existing capital assets.

b. The County shall not construct or acquire a public facility if it is unable to adequately provide for the subsequent annual operation and maintenance costs of the facility.

c. The County will ensure that adequate systems of internal controls exist, to provide reasonable assurance as to compliance with applicable laws, regulations, and covenants associated with outstanding debt.

d. The County will limit the use of Installment Financings, such as LOBs, to circumstances that require immediate action, or where there is a potential for significant benefit to the county.

e. The County will manage debt issuance to comply with the adopted debt limits and other financial policies and will evaluate such limits at least every five years.

f. The County will attempt to structure debt in the best and most appropriate manner, consistent with the financial policies of the County.

g. The County will monitor its outstanding debt in relation to existing conditions in the debt market and will refund any outstanding debt when sufficient cost savings can be realized or evaluate the use of interest rate swap agreements to achieve cost savings.

h. The County will utilize the Debt Service Fund to manage debt issuances and to make debt service and capital expenditures more *budget neutral* and intentional.

i. To reduce the impact of capital programs on future years, the County will fund a portion of its CIP on a pay-as-you-go basis by:

   - Appropriating a minimum amount of the property tax rate for capital projects, e.g., three cents or a proportional amount following revaluation of assessed property values;
   - Appropriating proceeds from all county land sales for capital projects.

   Pay-as-you-go funding will save money by eliminating interest expense on the funded projects. Pay-as-you-go capital appropriations improve financial flexibility in the event of sudden revenue shortfalls or emergency spending.

Refinancing of Outstanding Debt

The County in conjunction with its Financial Advisor will monitor the municipal bond market for opportunities to obtain interest savings by refunding outstanding debt. Current refundings of existing fixed rate debt will generally be considered when net present value savings meet or exceed 3% of the refunded par amount.

Additionally, the County may consider refinancing existing debt for reasons other than to achieve interest savings, including but not limited to mitigating risks associated with the County's debt portfolio.

Taxable advance refundings, synthetic refinancing opportunities, and other alternative structures will be evaluated on a case-by-case basis and must be determined to be in the best interest of the County by the Director of Finance and the County Manager.

The County will attempt to coordinate refunding transactions with the issuance of new debt to leverage combined issuance costs and create administrative efficiencies.

Credit Enhancement

Credit enhancements (letters of credit, liquidity providers, bond insurance, etc.) may be used to improve the overall cost of funds on a debt financing, mitigate potential risks to the County, or for other reasons deemed appropriate by the Finance Director and the County Manager. The County's Financial Advisor will provide an analysis establishing the additional value any credit enhancement.

Administration and Implementation

The County Manager and the Director of Finance are responsible for the administration and issuance of debt including the completion of specific tasks and responsibilities included in this policy. The County will evaluate the debt policy at least every five years.

Capital Planning and Debt Determination

The Mecklenburg County Capital Improvement Program (CIP) comprises the financing, acquisition, development, and implementation of improvement projects for the County's fixed assets. The CIP is a comprehensive five-year plan for land acquisition, and the development, modernization, or replacement of county-owned facilities, infrastructure, and equipment.

The Citizens Capital Budget Advisory Committee (CCBAC) is appointed by the Board of County Commissioners (BOCC) to review and make recommendations regarding proposed capital projects.

The County Manager and Director of Finance review, evaluate, and recommend capital projects for all functional areas through the CIP process. The BOCC adopts capital project ordinances to authorize projects in the CIP, and any amendments for capital plan updates. The BOCC also approves the capital budget to provide funding through the budget process. Available pay-as-you-go funding and debt issuance is allocated to fund the CIP, consistent with the Debt policy.

Where appropriate and consistent with the Debt Policy, the County will utilize the non-voted (two-thirds) bond authorization for bonds to fund projects, such as government facilities.

The County may use a combination of bonds and Installment Financings to finance capital assets. Installment Financings do not require voter approval but do require collateral as security.

Any capital item that has not been included in the CIP or capital budget process, but because of its critical or emergency nature, or is mandated immediately by either State or Federal requirements, will be considered for financing by installment purchase contract.

Debt Service Fund

The Debt Service Fund is established to provide separate dedicated funding for debt service management. The Debt Service Fund will be used to facilitate the payment of principal and interest for the County's general debt service and assist in the continued compliance with adopted debt policies. Annually, the County will appropriate to the Debt Service Fund a set tax rate through the annual budget process but be no lower than a minimum of nineteen cents of the property tax rate, or proportional amount as adjusted for revaluation of assessed property values. Funds appropriated can only be utilized for debt service or pay-as-you-go capital in the current or subsequent fiscal years. Accumulated fund balance should be limited to two years' non-property tax revenue. After the fund balance goal has been reached in the Debt Service Fund, a portion of the funds appropriated to the Debt Service Fund may be reallocated for use in pay-as-you-go capital funding.

Pay-As-You-Go Funding

To reduce the impact of capital programs on future years, the County will fund a portion of its approved CIP on a pay-as-you-go basis, by annually appropriating three cents of the property tax rate, or proportional amount as adjusted for revaluation of assessed property tax values. In addition, proceeds from all County land sales will be appropriated for approved CIP projects. These revenue sources will allow additional funding for CIP projects, and reduce the County's dependence on borrowing.

Issuance of Debt

The scheduling and amount of bond sales and installment purchase transactions will be recommended by the Director of Finance and the County Manager. The BOCC must approve the sale. These decisions will be based upon the identified cash flow requirements for each project to be financed, market conditions, and other relevant factors including the debt ratios. If the cash requirements for capital projects are minimal in any given year, the County may choose not to issue debt. Instead, the County may fund up-front project costs and reimburse these costs when financing is arranged. In these

circumstances, the County will take steps required to reimburse itself in accordance with IRS guidelines.

Debt service for each issue will be structured with a goal to level out the county's total debt service payments over the life of the debt portfolio and minimize the interest payments over the life of the issue. Structuring must take into consideration current market conditions and practices in the municipal finance market.

Method of Sale: There are four primary methods of issuing debt obligations: competitive sale, negotiated sale, private placement and bank loan. In a competitive sale, underwriters submit sealed bids and the underwriter or underwriting syndicate with the most favorable bid (as defined in the Notice of Sale), is awarded the bonds. In a negotiated sale, the underwriter or underwriting syndicate is selected by the County. The interest rates and underwriter's discount are negotiated, and the bonds are sold to investors during an order period. In a private placement, the County hires a placement agent to place a debt obligation with a specific investor or group of investors. A bank loan is a debt obligation sold directly to a bank or group of banks.

Generally, new fixed rate general obligation bond sales are required to be conducted on a competitive basis by the Local Government Commission (LGC), a division of the Office of the State Treasurer. Refunding Bonds and all other types of securities can be sold using a method of sale selected by the County. Variable rate bonds, revenue and special obligation bonds and Installment Financings will be sold on a negotiated basis with the underwriter selection determined through a competitive process. Underwriter(s) will be selected for each issue based on the experience and expertise necessary for that issue.

Legality

The County must receive an opinion acceptable to the market from a nationally recognized law firm that each financing transaction complies with applicable law and all agreements in connection with any financing are legal, valid and binding obligations of the County.

Interest Rate Exchange Agreements

Interest Rate Exchange Agreement shall mean a written contract entered into in connection with the issuance of County debt or in connection with County debt already outstanding with a counterparty to provide for an exchange of payments based upon fixed and/or variable interest rates. The County will govern the use of Interest Rate Exchange Agreements by the policy described in Attachment I to this debt management policy.

Continuing Disclosure and Relationships with Other Interested Parties

The County is committed to full and complete primary and secondary financial disclosure to interested parties including state and national regulators as well as those in the underwriting market, institutional investors, rating agencies and other market participants to enhance the marketability of the County's bonds. It will provide on-going disclosure information to established national information repositories and maintain compliance with disclosure standards promulgated by state and national regulatory agencies. The County will maintain good communications with investors and bond rating agencies to inform them about the County's financial position making the County's Comprehensive Annual Financial Report (CAFR), operating and capital improvements Budget and other required documents easily accessible.

Investment of Bond Proceeds

The County will invest its bond proceeds in compliance with North Carolina statutes, any restrictions within the related bond documents, and in compliance with the County's investment policy. Additionally, the County will invest the proceeds of any tax-exempt bond issue in compliance with IRS or other federal rules and regulations.

Arbitrage Rebate Reporting

The County will comply with all arbitrage rebate requirements as established by the Internal Revenue Service and all disclosure requirements established by the Securities and Exchange Commission. This effort includes tracking investment earnings on bond proceeds, calculating rebate payments in compliance with the tax law and remitting rebatable earnings to the federal government in a timely manner in order to preserve the tax exempt status of the County's outstanding debt issues.

Amended by the Board of County Commissioners, February 15, 2003
Amended by the Board of County Commissioners, April 15, 2003
Amended by the Board of County Commissioners, September 3, 2003
Amended by the Board of County Commissioners, November 5, 2008
Amended by the Board of County Commissioners, June 5, 2012
Amended by the Board of County Commissioners, May 20, 2014
Amended by the Board of County Commissioners, October 2, 2018

MECKLENBURG COUNTY
DEBT POLICY

Attachment I: Interest Rate Exchange Agreement Policy

Mecklenburg County
Interest Rate Exchange Agreement Policy

This policy will govern the use by Mecklenburg County (the "County") of Interest Rate Exchange Agreements. "Interest Rate Exchange Agreement" shall mean a written contract entered into in connection with the issuance of County debt or in connection with County debt already outstanding with a counterparty to provide for an exchange of payments based upon fixed and/or variable interest rates. The failure by the County to comply with any provision of this policy will not invalidate or impair any Interest Rate Exchange Agreement.

The Conditions Under Which Interest Rate Exchange Agreements May Be Entered Into

Purposes

Interest Rate Exchange Agreements may be used for the following purposes only to:

a. achieve significant savings as compared to a product available in the bond market if the use of derivatives helps to achieve diversification of a particular bond offering;
b. enhance investment returns within prudent risk guidelines;
c. prudently hedge risk in the context of a particular financing or the overall asset/liability management of the County;
d. incur variable rate exposure within prudent guidelines;
e. achieve more flexibility in meeting overall financial objectives than available in conventional markets; and
f. accomplish a financial objective not otherwise obtainable using traditional financing methods.

Legality

The County must receive an opinion acceptable to the market from a nationally recognized law firm that the Interest Rate Exchange Agreement is a legal, valid and binding obligation of the County and entering into the transaction complies with applicable law.

Speculation

Interest Rate Exchange Agreements shall not be used for speculative purposes. Associated risks will be prudent risks that are appropriate for the County to take.

Methods by Which Such Contracts Shall be Solicited and Procured
In general, the County should procure Interest Rate Exchange Agreements by competitive bidding. The County shall determine which parties it will allow to participate in a competitive transaction. The County has the right to accept matching bids to diversify counterparty risk or reward firms for ideas and work performed. The parameters for the bid must be disclosed in writing to all potential bidders.

Notwithstanding the above, the County may procure Interest Rate Exchange Agreements by negotiated methods when the County makes a determination that, due to the size or complexity of a given swap, a negotiated transaction would result in the most favorable pricing and terms or innovation.

To facilitate the procurement of Interest Rate Exchange Agreements, the County will engage an independent financial advisory firm to assist in the price negotiations, in the development of terms and in risk assessment. The County shall obtain an independent opinion that the terms and conditions of the Interest Rate Exchange Agreement reflect a fair market value of such agreement as of the date of its execution.

Form and Content of Interest Rate Exchange Agreements
To the extent possible, the Interest Rate Exchange Agreements entered into by the County shall contain the terms and conditions set forth in the International Swap and Derivatives Association, Inc. ("ISDA") Master Agreement, including any schedules and confirmation. The schedule should be modified to reflect specific legal requirements and business terms desired by the County.

The County shall consider including provisions that permit the County to assign its rights and obligations under the Interest Rate Exchange Agreement and to optionally terminate the agreement at its market value at any time. In general, the counterparty shall not have the right to optionally terminate an agreement.

Events of Default
Events of default of a counterparty shall include the following:

a. failure to make payments when due;
b. material breach of representations and warranties;
c. illegality;
d. failure to comply with downgrade provisions; and/or
e. failure to comply with any other provisions of the agreement after a specified notice period.

The County will have the right to terminate the agreement upon an event of default by the counterparty. Upon such termination, the counterparty will be the "defaulting party" for purposes of calculating the termination payment owed.

Aspects of Risk Exposure Associated with Such Contracts

Before entering into an Interest Rate Exchange Agreement, the County shall evaluate all the risks inherent in the transaction. These risks to be evaluated could include:

a. counterparty risk – the risk of a payment default on a swap by an issuer's counterparty;
b. termination risk – the risk that a swap has a negative value and the issuer owes a breakage fee if the contract has to be terminated;
c. rollover risk – the risk of a failed remarketing or auction with respect to any variable rate bonds associated with a swap; or the risk that an issuer cannot secure a cost-effective renewal of a letter or line of credit;
d. basis risk - the risk that floating rate cash flow streams may diverge from each other;
e. tax event risk – the risk that the spread between taxable and tax-exempt rates will change as a result of changes in income tax laws or other conditions; and
f. amortization risk – the risk that the amortization of the swap will not be fully integrated with the amortization of the underlying bonds.

The County shall endeavor to diversify its exposure to counterparties. To that end, before entering into a transaction, it should determine its exposure to the relevant counterparty or counterparties and determine how the proposed transaction would affect the exposure. The exposure should not be measured solely in terms of notional amount, but also how changes in interest rates would affect the County's "Value at Risk" exposure for outstanding agreements.

Counterparty Selection Criteria

The County may enter into an Interest Rate Exchange Agreement if the counterparty has at least two long term unsecured credit ratings in the AA category from Fitch, Moody's, or S&P, and the counterparty has demonstrated experience in successfully executing Interest Rate Exchange Agreements. If after entering into an agreement the ratings of the counterparty are downgraded below the ratings required, then the agreement shall be subject to termination unless (a) the counterparty provides either a substitute guarantor or assigns the agreement, in either case, to a party meeting the rating criteria reasonably acceptable to the County or (b) the counterparty (or guarantor) collateralizes the Interest Rate Exchange Agreement in accordance with the criteria set forth in this Policy and the Interest Rate Exchange Agreement.

Provisions for Collateralization

Should the rating of the counterparty, or if secured, the entity unconditionally guaranteeing its payment obligations not satisfy the requirements of the Counterparty

Selection Criteria, then the obligations of the counterparty shall be fully and continuously collateralized by (a) direct obligations of, or obligations the principal and interest on which are guaranteed by, the United States of America or (b) direct obligations of U.S. Agencies and such collateral shall be deposited with the County or an agent thereof. The specific collateral requirements for each Interest Rate Agreement shall be set forth in the corresponding swap documentation.

Long-Term Implications
In evaluating a transaction involving the use of Interest Rate Exchange Agreements, the County shall review long-term implications associated with entering into Interest Rate Exchange Agreements, including costs of borrowing, historical interest rate trends, variable rate capacity, credit enhancement capacity, opportunities to refund related debt obligations and other similar considerations.

Methods to be Used to Reflect Such Contracts in the County's Financial Statements
The County shall reflect the use of Interest Rate Exchange Agreements on its financial statements in accordance with generally accepted accounting principles.

Monitoring
The County shall monitor the performance of Interest Rate Exchange Agreements and may employ a financial advisor to assist in evaluating the effectiveness of its Agreements. A written report, provided at a minimum quarterly, shall include at least:

a. preparing a description of each contract, including a summary of its terms and conditions, the notional amount, rates, maturity and other provisions thereof;
b. determining any amounts which were required to be paid and received, and that the amounts were paid and received;
c. determining that each counterparty is in compliance with it rating requirements;
d. determining that each counterparty is in compliance with the downgrade provisions, if applicable (See Counterparty Selection Criteria);
e. assessing the counterparty risk, termination risk, basis risk and other risks, which shall include the marked to market value for each counterparty and relative exposure compared to other counterparties and a calculation of the County's Value at Risk for each counterparty; and
f. determining, at least quarterly, that all posted collateral, if required, has a net market value of at least the collateral in the Interest Rate Agreement.