City of Victoria, Texas

Post Bond Issuance Compliance Policy and Written Procedures

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I. **INTRODUCTION**

The City of Victoria (the “City”) issues debt obligations that are considered “Tax-advantaged bonds”, these include tax-exempt obligations and direct-pay obligations that receive preferential federal tax treatment (collectively referred to herein as the “Bonds”). The preferential tax treatment afforded to the Bonds results in lower borrowing costs for the City. Because of the preferential tax treatment afforded to the Bonds, the City’s Bonds are subject to applicable federal tax requirements both at the time of their issuance and for as long as the Bonds remain outstanding, including any refunding of those original Bonds. The City’s failure to comply with any applicable federal tax requirements with respect to the City’s Bonds could potentially jeopardize the preferential tax status of those Bonds.

II. **POST-ISSUANCE COMPLIANCE WITH FEDERAL TAX REQUIREMENTS**

Compliance with certain applicable federal tax requirements normally occurs at the closing of a Bond transaction, while other federal tax requirements require ongoing monitoring after the issuance of the Bonds. Post-issuance federal tax requirements generally fall into two categories: (1) qualified use of proceeds and financed property and (2) arbitrage yield restriction and rebate. Qualified use requirements require monitoring of the various direct and indirect uses of Bond-financed property over the life of the Bonds and calculating the percentages of nonqualified uses. Arbitrage requirements also require monitoring over the life of the Bonds to determine whether both the yield on investments allocated to the Bonds are properly restricted and whether the City must make a yield reduction payment and/or a rebate payment.

The ongoing nature of post-issuance compliance requirements applicable to the City’s Bonds requires the City to actively monitor compliance throughout the entire period the City’s Bonds remain outstanding. This due diligence will significantly improve the City’s ability to prevent violations from occurring, or timely correct identified violations (when prevention is not possible), to ensure the continued tax-advantaged status of the Bonds.

III. **THE CITY’S GOAL IN ESTABLISHING WRITTEN PROCEDURES**

The City’s goal of establishing and following written procedures is to preserve the preferential tax status of its Bonds.

IV. **RESPONSIBLE PERSON**

The City’s chief financial officer, which is currently the Director of Finance, is hereby designated as the City’s "Responsible Person." The Responsible Person shall receive appropriate training regarding the City's accounting system, contract intake system, facilities management and other systems necessary to track the investment and expenditure of the proceeds and the use of the facilities financed or refinanced with the proceeds of the Bonds. The Responsible Person will be assisted by the staff of the City’s Finance Department and by other City staff and officials when appropriate. The Responsible Person will also be assisted in carrying out post-issuance compliance requirements by the following organizations:
(a) **Bond Counsel** (the law firm primarily responsible for providing bond counsel services for the City);

(b) **Financial Advisor** (the organization primarily responsible for providing financial advisor services to the City);

(c) **Paying Agent** (the person, organization, or City officer primarily responsible for providing paying agent services for the City); and

(d) **Rebate Analyst** (the organization primarily responsible for providing rebate analyst services for the City – whether done internally or contracted with a third party provider).

The Responsible Person shall be responsible for assigning post-issuance compliance responsibilities to staff of the City’s Finance Department, other staff of the City, Bond Counsel, Financial Advisor, Paying Agent, and Rebate Analyst. The Responsible Person shall utilize such other professional service organizations as are necessary to ensure compliance with the post-issuance compliance requirements of the City. The Responsible Person shall provide training and educational resources to City staff who are responsible for ensuring compliance with any portion of the post-issuance compliance requirements set forth in these written procedures.

V. **Arbitrage Rebate and Monitoring**

Arbitrage occurs when the proceeds of a Bond issue are used to acquire investments that earn a yield higher than the interest payable to the bondholders of such Bonds. As set forth herein, in these situations, the Internal Revenue Service (the “**IRS**”) assesses a penalty equal to one hundred percent (100%) of the excess earnings, subject to certain exceptions. The City will comply with the arbitrage requirements established by Section 148 of the Internal Revenue Code (the “**Code**”).

(a) **Arbitrage Rebate.**

1. **Rebate.** The arbitrage that must be rebated to the U.S. Department of the Treasury is based on the excess (if any) of the amount actually earned on non-purpose investments over the amount that would have been earned if those investments had a yield equal to the yield on the Bonds, plus any income attributable to such excess. Under Section 1.148-3(b) of the Treasury regulations, the future values of all earnings received and payments made with respect to non-purpose investments are included in determining the amount of rebate due.

2. **Procedure for Compliance.** The Responsible Person shall assure that, unless excepted from rebate and yield restriction under section 148(f) of the Code, excess investment earnings are computed and paid to the U.S. government at such time and in such manner as directed by the IRS (A) at least every 5 years after the date of delivery of the Bonds and (B) within 30 days after the date the Bonds are retired.
(c) Arbitrage Monitoring.

(1) With respect to the investment and expenditure of the proceeds of all Bonds, the Responsible Person will:

(a) monitor all amounts deposited into a sinking fund or funds, to assure that the maximum amount invested at a yield higher than the yield on the Bonds does not exceed an amount equal to the debt service on the Bonds in the succeeding 12 month period plus a carryover amount equal to one-twelfth of the principal and interest payable on the Bonds for the immediately preceding 12-month period; and

(2) With respect to the investment and expenditure of the proceeds of Bonds issued for new projects, and in addition to the requirements set forth above in Section V(b) (1), the Responsible Person will:

(a) instruct the appropriate person or persons that the construction, renovation or acquisition of the facilities financed with the Bonds must proceed with due diligence and that binding contracts for the expenditure of at least 5% of the proceeds of the Bonds will be entered into within six (6) months of the date of delivery of the Bonds (the "Issue Date");

(b) monitor that at least 85% of the proceeds of the Bonds to be used for the construction, renovation or acquisition of any facilities are expended within three (3) years of the Issue Date;

(c) restrict the yield of the investments to the yield on the Bonds after three (3) years of the Issue Date;

(d) ensure that no more than 50% of the proceeds of the Bonds are invested in an investment with a guaranteed yield for four years or more; and

(e) maintain any official action of the City (such as a reimbursement resolution) stating its intent to reimburse with the proceeds of the Bonds any amount expended prior to the Issue Date for the acquisition, renovation or construction of the facilities.

(3) With respect to the investment and expenditure of the proceeds of Bonds issued to refund existing Bonds, and in addition to the requirements set forth above in Section V(b) (1), the Responsible Person will:

(a) monitor the actions of the escrow agent to ensure compliance with the applicable provisions of the escrow agreement, including with respect to reinvestment of cash balances.
VI. PRIVATE BUSINESS USE

(a) General.

Generally, the facilities financed or refinanced with the proceeds of the Bonds (the “Project”) must be owned and operated by the City (or another state or local governmental entity). At all times while the Bond issue is outstanding, no more than 10% of the Bond proceeds or the Project may be used, directly or indirectly, in a trade or business carried on by a person other than a state or local governmental unit (referred to as “Private Use”). Such amount is reduced to 5% if the Private Use is unrelated and disproportional. Generally, Private Use consists of any contract or other arrangement, including leases, management contracts, operating agreements, guarantee contracts, take or pay contracts, output contracts or research contracts, which provides for use by a person who is not a state or local government on a basis different than the general public. Private Use may include: (i) owning, leasing, providing services, operating, or managing the Project; (ii) acquiring the output (or throughput) of the Project; or (iii) acquiring or using technology developed at the Project.

The Project may be used by any person or entity, including any person or entity carrying on any trade or business, if such use constitutes “General Public Use”. General Public Use is any arrangement providing for use that is available to the general public at either no charge or on the basis of rates that are generally applicable and uniformly applied. The Responsible Person will monitor all leases and subleases, and other forms of disposition of property that has been financed with Bonds. Prior to entering into any lease or sublease or otherwise disposing of a Bond-financed property, the Responsible Person will consult with Bond Counsel to determine the impact, if any, such lease or sublease would have on the tax status of the Bonds.

(b) Procedure for Compliance.

With respect to the use of the facilities financed or refinanced with the proceeds of the Bonds, the Responsible Person will:

(i) monitor the date on which the facilities are substantially complete and available to be used for the purpose intended;

(ii) monitor whether, at any time the Bonds are outstanding, any person, other than the City, the employees of the City, the agents of the City or members of the general public has any contractual right (such as a lease, purchase, management or other service agreement) with respect to any portion of the facilities;

(iii) monitor whether, at any time the Bonds are outstanding, any person, other than the City, the employees of the City, the agents of the City or members of the general public has a right to use the output of the facilities (e.g., water, gas, electricity);

(iv) monitor whether, at any time the Bonds are outstanding, any person, other than the City, the employees of the City, the agents of the City or members of the general public has a right to use the facilities to conduct or to direct the conduct of research;

(v) determine whether, at any time the Bonds are outstanding, any person, other than the City, has a naming right for the facilities or any other contractual right granting an intangible benefit;
(vi) determine whether, at any time the Bonds are outstanding, the facilities are sold or otherwise disposed of; and

(vii) take such action as is necessary to remediate any failure to maintain compliance with the covenants contained in the ordinance authorizing the issuance of the respective Bonds related to the public use of the facilities.

VII. RETURN FILINGS

The Responsible Person will ensure that the applicable information return (e.g., IRS Form 8038-G, 8038-GC, or any successor forms) is timely filed with the IRS. A separate Form 8038-G must be filed for each issue of Bonds not later than the 15th day of the second calendar month after the close of the calendar quarter in which the Bonds are issued.

VIII. RECORDKEEPING AND RECORD RETENTION

The IRS requires the City to maintain sufficient records to support Bondholders’ continued exclusion of interest on the Bonds. Specifically, the Responsible Person shall keep record of:

(a) the Bond transcript of proceedings;
(b) all ordinances and resolutions (including reimbursement resolutions) and minutes pertaining to the projects financed if not included in the bond transcript;
(c) all bond yield computations including supporting certificates and investment records (including trustee records) pertaining to proceeds of the Bonds, investment agreements and related bidding documents, swap documents, rebate reports and rebate payments;
(d) all documents pertaining to the expenditure of Bond proceeds for the acquisition, construction or renovation of Bond financed property including any trustee records, requisitions, reimbursements, draw schedules, draw requests, construction contracts, invoices, bills, land/project related appraisals, payment records, requisition statements, reimbursement records, cancelled checks, a final schedule of property financed by the Bonds and final allocations of Bond proceeds;
(e) all formal elections made for the Bond financing (e.g., an election to employ an accounting methodology other than specific tracing) all records of purchase, lease or sale of Bond financed property including any ownership documentations such as joint venture arrangements, limited liability corporation arrangements or partnership arrangements;
(f) all management contracts and other service agreements, research contracts, and naming rights contracts;
(g) all accounting audits for Bond financed property;
(h) any other workpapers provided to the Rebate Consultant;
(i) all information reports filed for the Bonds; and
(j) all documentation pertaining to any prior IRS examination of City and/or Bonds of the City.
The Responsible Person will maintain or cause to be maintained all records relating to the investment and expenditure of the proceeds of the Bonds and the use of the facilities financed or refinanced thereby for a period ending three (3) years after the complete extinguishment of the Bonds. If any portion of the Bonds is refunded with the proceeds of another series of tax-exempt obligations, such records shall be maintained until the three (3) years after the refunding obligations are completely extinguished. Such records can be maintained in paper or electronic format.

**IX. ANNUAL REVIEW OF POST ISSUANCE COMPLIANCE PROCEDURES**

The Responsible Person, on an annual basis and with the assistance of outside consultants of the City as deemed necessary or appropriate by the Responsible Person, will review these written procedures to confirm their continued applicability and effectiveness in preserving the preferential tax status of the City’s Bonds.