Council Meeting Date: October 17, 2016 **Agenda Item**: 8(b)

CITY COUNCIL AGENDA ITEM

CITY OF SHORELINE, WASHINGTON

AGENDA TITLE:	Discussion of Resolution No. 396 Delegating Authority to Designate Expenditures for Reimbursement from Bonds that may be Authorized and Approved in the Future
DEPARTMENT:	Administrative Services Department
PRESENTED BY:	Sara Lane, Administrative Services Director
ACTION:	____ Ordinance ____ Resolution ____ Motion __X__ Discussion ____ Public Hearing

PROBLEM/ISSUE STATEMENT:
Internal Revenue Service (IRS) regulations allow the City within certain restrictions to reimburse eligible expenditures that have been contributed from other funds prior to bond issuance. The declaration of intent to reimburse from tax-exempt bond proceeds must be done within 60 days of the payment of the original expenditure of the funds, and, with limited exceptions, the reimbursement from bonds must be completed within three years of the date of the original expenditure.

Proposed Resolution No. 396 allows the City Manager or her designee to certify eligible expenses within 60 days of being incurred. The certification would become back-up documentation to the future reimbursement from bond proceeds. Council will discuss proposed Resolution No. 396 tonight, and it will be brought back to Council for potential adoption on November 7, 2016.

RESOURCE/FINANCIAL IMPACT:
Without appropriate authorization to reimburse expenditures from potential future bond proceeds the City may incur higher interest and or arbitrage charges that could be avoided with timely documentation of potentially reimbursable expenses. The actual impact would be dependent on several factors including market rate of return, the amount of the bond issue and the amount of potentially reimbursable expenses.

RECOMMENDATION

Staff recommends that Council review proposed Resolution No. 396 delegating authority to designate expenditures for reimbursement from bonds that may be authorized and approved in the future and direct staff to return with the resolution for Council adoption on November 7, 2016.

Approved By: City Manager ***DT*** City Attorney ***MK***

BACKGROUND

Issuers of governmental bonds, qualified 501(c)(3) bonds, and private activity bonds issued for the purpose of financing governmentally owned facilities, may allocate all or a portion of the proceeds of such bonds to the reimbursement of expenditures made prior to the date of issuance if certain rules are followed. These bonds are referred to as "reimbursement bonds." If the rules are followed, the portion of the proceeds allocated to the reimbursement will be considered "spent" when the allocation is made, and will not be subject to the general arbitrage and rebate rules imposed under the Internal Revenue Code of 1986, as amended (the "Code") and the federal tax regulations (the "Regulations").

DISCUSSION

During the financial planning process, the City may identify the potential need for future debt funding for a project. The City tries to time the issuance of the debt carefully to avoid unnecessary interest and administrative costs.

Once staff issues the debt, the City begins to incur interest costs and has monitoring requirements including the need to ensure that the City is not earning more interest than it is paying (called Arbitrage). Compliance monitoring continues throughout the life of a bond, but Arbitrage monitoring is only required until the bond proceeds are fully expended.

The IRS regulations would allow the City to identify potential reimbursable expenses in advance, thus allowing the City to have maximum flexibility on the timing of the Debt without delaying project expenditures. A good example of where this would be beneficial would be future work on the North Maintenance Facility, where timing of design and construction is unknown and immediate costs needed to complete planning is needed to proceed.

Proposed Resolution No. 396 (Attachment A) allows the City Manager or her designee to certify eligible expenses within 60 days of being incurred. The certification would become back-up documentation to the future reimbursement from bond proceeds. The IRS has developed rules related to reimbursement to prevent abuse of this management tool. These are described at Attachment B.

RESOURCE/FINANCIAL IMPACT

Without appropriate authorization to reimburse expenditures from potential future bond proceeds the City may incur higher interest and or arbitrage charges that could be avoided with timely documentation of potentially reimbursable expenses. The actual impact would be dependent on several factors including market rate of return, the amount of the bond issue and the amount of potentially reimbursable expenses.

RECOMMENDATION

Staff recommends that Council review proposed Resolution No. 396 delegating authority to designate expenditures for reimbursement from bonds that may be authorized and approved in the future and direct staff to return with the resolution for Council adoption on November 7, 2016.

ATTACHMENTS

Attachment A – Proposed Resolution No. 396, including Exhibit A
Attachment B – Municipal Bonds: Reimbursement Rules

RESOLUTION NO. 396

A RESOLUTION OF THE CITY OF SHORELINE, WASHINGTON, APPOINTING THE CITY MANAGER FOR THE PURPOSE OF DESIGNATING CERTAIN EXPENDITURES FOR REIMBURSEMENT FROM BONDS THAT MAY BE AUTHORIZED AND APPROVED BY THE CITY FOR ISSUANCE IN THE FUTURE.

WHEREAS, the City of Shoreline, Washington (the "City") issues tax-exempt obligations, including bonds, notes, and leases from time to time for the purpose of financing its governmental activities; and

WHEREAS, the United States Department of the Treasury has published regulations (the "Regulations") governing the ability of the City to use the proceeds of tax-exempt obligations for reimbursement of prior expenditures; and

WHEREAS, the Regulations require that a governmental entity declare its intent ("Official Intent") to issue tax-exempt bonds to reimburse itself for expenditures made prior to the issuance of such bonds before the expenditures are incurred and such Official Intent may be made by a representative of the entity authorized or designated for such purposes;

NOW, THEREFORE, THE CITY COUNCIL OF THE CITY OF SHORELINE HEREBY RESOLVES:

Section 1. The City Council hereby appoints and designates the City Manager, or his or her designee (the "Authorized Representative"), as the official responsible for issuing statements of Official Intent in compliance with Treasury Regulation Section 1.150-2. Upon a determination by the Authorized Representative that the costs of a particular capital project may be reimbursed from the proceeds of tax-exempt obligations of the City, the Authorized Representative is authorized and directed to execute a certificate of Official Intent, substantially in the form attached hereto as Exhibit A. Each certificate so executed shall become a part of the official records of the City available for public inspection and review.

Section 2. The adoption of this resolution and any statement of Official Intent made by the Authorized Representative shall not obligate the City to issue tax-exempt obligations. The issuance of such obligations shall require separate and additional official approval by the City Council.

Section 3. This resolution shall take effect and be in full force immediately after passage by the City Council.

ADOPTED BY THE CITY COUNCIL ON NOVEMBER 7, 2016.

____
Mayor Christopher Roberts

ATTEST:

____
Jessica Simulcik Smith
City Clerk

APPROVED AS TO FORM:

____
Pacifica Law Group LLP, Bond Counsel

EXHIBIT A

FORM OF OFFICIAL INTENT CERTIFICATE

Pursuant to Resolution No. 396 of the City of Shoreline, Washington (the "City"), the undersigned, City Manager, or _______________, as designee of the City Manager, hereby states as follows:

Section 1. The City reasonably expects to reimburse the expenditures described herein with the proceeds of debt to be incurred by the City (the "Reimbursement Bonds").

Section 2. The maximum principal amount of Reimbursement Bonds expected to be issued is $[__________].

Section 3. The expenditures with respect to which the City reasonably expects to be reimbursed from the proceeds of Reimbursement Bonds will be made from the City's [___________________] Fund for project costs related to the [brief description of the project].

Dated this ____ day of __________, 20____.

____
City Manager
____________, as designee of the City Manager

Attachment B

PACIFICA
LAW GROUP

Municipal Bonds: Reimbursement Rules

Issuers of governmental bonds, qualified 501(c)(3) bonds, and private activity bonds issued for the purpose of financing governmentally owned facilities, may allocate all or a portion of the proceeds of such bonds to the reimbursement of expenditures made prior to the date of issuance if certain rules are followed. These bonds are referred to as "reimbursement bonds." If the rules are followed, the portion of the proceeds allocated to the reimbursement will be considered "spent" when the allocation is made, and will not be subject to the general arbitrage and rebate rules imposed under the Internal Revenue Code of 1986, as amended (the "Code") and the federal tax regulations (the "Regulations"). The following is a summary of the general requirements for qualifying reimbursements.

Official Intent Declaration Requirement. The issuer, or in limited circumstances the ultimate borrower, must declare its "official intent" to reimburse itself not later than 60 days after payment of the original expenditure. The declaration of official intent may be made before any expenditures are made, and will essentially "start the clock" for purposes of reimbursement. The official intent declaration must include the following requirements:

- The declaration may be made in any reasonable form, including a resolution or other legislative authorization. The legislative action may specifically declare the intent to reimburse or may delegate to an individual the authority to make the declaration.
- The declaration of official intent must:
    - contain a general functional description of the project, property or program to be financed by the reimbursement bonds (for instance, highway capital improvement program or school building renovation). The project description is sufficient if it identifies, by name and functional purpose, the fund or account from which the original expenditure is paid (for instance, parks and recreation fund-recreational facility capital improvement program); and
    - state the maximum principal amount of the obligations expected to be issued for the project.

  The Regulations allow for reasonable deviations in the project description, so long as the actual project is reasonably related in function to the described project.
- The declaration of intent must be "reasonable." A declaration of intent will be considered reasonable if, on the date of the declaration, the issuer or ultimate borrower had a reasonable expectation that it would reimburse the original expenditure with proceeds of reimbursement bonds. Reasonableness is based on the relevant facts and circumstances, including the issuer's history of making declarations and actually reimbursing expenditures. For instance, declarations of intent made as a matter of course or in amounts substantially in excess of the amounts expected to be necessary for the project are not reasonable. Similarly, a pattern of failing to reimburse original

expenditures covered by declarations of official intent (other than due to extraordinary circumstances) is evidence of unreasonableness.

Eligible Expenditures. Generally, the expenditures to be reimbursed must be "capital expenditures." A capital expenditure is any cost of a type that is properly chargeable to a capital account (or would be so chargeable with a proper election) under general federal income tax principles. The Regulations also include extraordinary working capital expenditures, bond costs of issuance, grants, qualified student loans, and qualified mortgage loans as expenditures eligible for reimbursement. Non-extraordinary working capital expenditures are typically not eligible. The determination of whether an expenditure is a capital expenditure is made at the time the expenditure is made, not at the time of issuance of the reimbursement bonds.

Reimbursement Period. The reimbursement bonds must be issued and proceeds must be allocated to reimburse the issuer or conduit borrower not later than 18 months after the *later* of:

- The date on which the original expenditure is paid, or
- The date that the project to be financed was placed in service, but in no event more than three years after the original expenditure is paid.

Special rules apply for governmental issuers that expect to issue no more than $5 million of governmental bonds in any calendar year, and for long term construction projects.

Proceeds of reimbursement bonds will be "allocated" to reimbursement once there is written evidence of an issuer's (or conduit borrower's) use of the proceeds to reimburse a prior expenditure. An allocation made within 30 days of issuance of the reimbursement bonds may be treated as made on the date of issuance of the reimbursement bonds.

Special Exceptions. The official intent declaration requirement and the timing of issuance of reimbursement bonds do not apply to:

- costs of issuance for a bond issue;
- an amount not in excess of the lesser of $100,000 or 5% of the bond proceeds; or
- preliminary expenditures not in excess of 20% of the aggregate issue price of the related reimbursement bond issue. Preliminary expenditures include architectural, engineering, surveying, soil testing, reimbursement bond issuance, and similar costs that are incurred before commencement of acquisition, construction or rehabilitation of the financed property. Land acquisition, site preparation and other costs incident to commencement of construction do not constitute preliminary expenditures.

Original expenditures in these categories may be reimbursed with bond proceeds without following the reimbursement bond rules.