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## **Tennessee State Funding Board Guidelines**

### **Adopting a Debt Management Policy – Requirements, Objectives, and Best Practices**

#### **I. Debt Management Policy**

The State Funding Board is authorized to develop model finance policies for use by public entities pursuant to Tenn. Code Ann. § 9-21-134. The following guidelines have been developed for public entities in Tennessee by requiring the adoption of a policy that supports responsible debt management. These guidelines should be followed when preparing, adopting, reviewing, and amending debt management policies.

Adopting financial policies can help entities:

1. Make better financial decisions;
2. Provide clear objectives for staff;
3. Demonstrate strong financial management practices to credit rating agencies; and
4. Distinguish policy decisions from transaction decisions.

Financial policies do not prevent unforeseen or negative events from occurring, nor do they prevent poor financial decisions. However, public entities that have sound financial policy guidelines in place can address situations proactively before they occur and minimize risks.

All public entities that incur or issue debt must have a debt management policy, adopted by its governing board, that contains the minimum requirements as described below. The policy needs to address the types of debt the entity utilizes or plans to utilize for its financing.

Prior to adopting a policy, members of the public entity's governing board should have an understanding of public finance so that they participate in policy discussions and gain more value from external professional assistance; however, even if professional assistance is utilized, the entity is solely responsible for the development, adoption, and implementation of the policy.

There are four guiding principles that are foundational to all debt management policies:

1. Understand the transaction;
2. Explain to citizens what is being considered;
3. Avoid conflicts of interest; and
4. Disclose costs and risks.

These principles have been incorporated into the following requirements.

### **Debt Management Policy - Minimum Requirements**

Debt management policies, including any revisions, must be filed with the Comptroller of the Treasury at LGF@cot.tn.gov.

The policy should address the following:

1. The information that is to be provided to the public, governing body, and all stakeholders regarding:
  - a. the decision to issue debt, how debt will be structured and sold, and all costs involved in issuing debt (See glossary for a definition of costs.);
  - b. the selection process for professionals who provide services related to debt issuance;
  - c. conflicts of interest;
  - d. all ongoing debt and related costs (including interest and recurring administrative costs); and
  - e. federal and regulatory compliance issues.
2. A process for legal review of proposed debt to be issued to ensure the public entity is both authorized to issue the debt and in compliance with applicable state, local, and/or federal laws.
3. The overall financial management strategy and the purpose for issuing debt.
4. Transparency, the hiring of financial professionals, and conflicts of interest. (See Appendix A for minimum language to be included.
5. Terms of the debt issue that are required to be disclosed, such as maturity, interest rate, and scheduled debt service. In no event may payment of either principal or interest exceed the useful life of the asset financed.
6. Whether deferral of payment of principal (or backloading) is allowed. If permitted, the policy must require specific justification for the repayment structure. If local governments issue debt with a balloon structure, the government must comply with the requirements of Tenn. Code

Ann. § 9-21-133, which requires approval by the Tennessee Comptroller's Office prior to the debt being issued.

7. Maximum levels or amounts of debt that the public entity may issue per security type. This may be based on locally adopted economic indicators, such as debt per capita, a comparison of debt to property values, or debt service as a percentage of revenues or expenditures. The policy should require that this limitation be evaluated before additional debt is issued and reviewed periodically with the governing body.
8. How the public entity addresses risks associated with debt instruments that include:
  - a. a put (or tender) options (a provision where the holder of the debt can force repayment with a limited notice period);
  - b. an interest rate reset provisions; or
  - c. a variable interest rate.

This may include setting a maximum amount, level, or percentage of debt the public entity is willing to have outstanding at any time that includes any of the above risks and maintaining reserves sufficient to safeguard against risks. Debt issued by local governments with a variable interest rate, rate reset provision or put option must be approved by the Comptroller's Office prior to being issued as required by Tenn. Code Ann. § 9-21-409.

The State, as well as a few larger local governments, utilize commercial paper programs and revolving lines of credit to finance capital projects to be refinanced at a later date with long-term debt. Commercial paper is issued at variable rates, with terms ranging from 1 to 270 days, and at maturity commercial paper may be reissued at a different interest rate and with different terms or repaid. If public entities plan to issue commercial paper the policy should describe the program (including the type of commercial paper authorized to be issued, regular and/or extendable), outline the risks involved, and how the public entity manages the risks. The percentage of debt allowed to be outstanding with a variable interest rate generally excludes commercial paper due to its inherent short-term nature.

9. A plan for regularly reviewing and amending the policy. At a minimum, the policy must be reviewed each time there are legislative changes that impact the policy and when there is a change in the administration or governing body.

A list of resources and a glossary are provided to assist with developing debt management policies. (See Appendix B and Appendix C.)

*Effective November 1, 2009, and as amended June 23, 2025.*

# Appendix A

## Minimum Language

### 1. Transparency

- The Entity shall comply with legal requirements for notice and for public meetings related to debt issuance. In the interest of transparency, all costs (including interest, issuance, continuing, and one-time) shall be disclosed to the citizens/members, governing body, and other stakeholders in a timely manner. *(The method for disclosure of costs and other information, including documentation of compliance with the policy, shall be developed and outlined in the policy.)*

### 2. Professionals

- The Entity shall require all professionals engaged in the process of issuing debt to clearly disclose all compensation and consideration received related to services provided in the debt issuance process by both the Entity and the lender or conduit issuer, if any. This includes “soft” costs or compensations in lieu of direct payments.
- Counsel<sup>1</sup>: The Entity shall enter into an engagement letter agreement with each lawyer or law firm representing the Entity in a debt transaction. *(No engagement letter is required for any lawyer who is an employee of the Entity or lawyer or law firm which is under a general appointment or contract to serve as counsel to the Entity. The Entity does not need an engagement letter with counsel not representing the Entity, such as underwriters’ counsel.)*
- Financial Advisor<sup>2</sup>: If the Entity chooses to hire financial advisors, the Entity shall enter into a written agreement with each person or firm serving as financial advisor for debt management and transactions.
- Underwriter: If there is an underwriter, the Entity shall require the Underwriter to clearly identify itself in writing (e.g., in a response to a request for proposals or in promotional materials provided to an issuer) as an underwriter and not as a financial advisor from the earliest stages of its relationship with the Entity with respect to that issue. The Underwriter must clarify its primary role as a purchaser of securities

<sup>1</sup> The requirement for an engagement letter does not apply to any lawyer who is an employee of the Entity or any lawyer or law firm under a general appointment as counsel to the Entity and not serving as bond counsel for the transaction.

If bond counsel for a debt transaction does not represent the Entity in that transaction, the Entity will enter into a fee payment letter agreement with such lawyer or law firm specifying:

- a. the party represented in the debt transaction; and
- b. the Entity’s obligation with respect to the payment of such lawyer or law firm’s fees and expenses.

<sup>2</sup>For new issues of debt which constitutes a “security” for which the Time of Formal Award (as defined in Rule G-34(a)(ii)(C)(1)(a)) occurs after November 27, 2011, the Municipal Securities Rulemaking Board has prohibited broker, dealer or municipal securities dealer serving as a financial advisor to an issuer for a particular issue from switching roles and underwriting the same issue. Policies must be adjusted to comply with amended Rule G-23 as it applies to securities, including exceptions to the prohibition.

in an arm's-length commercial transaction and that it has financial and other interests that differ from those of the Entity. The Underwriter in a publicly offered, negotiated sale shall be required to provide pricing information both as to interest rates and to takedown per maturity to the governing body (*or its designated official*) in advance of the pricing of the debt.

### 3. Conflicts

- Professionals involved in a debt transaction hired or compensated by the Entity shall be required to disclose to the Entity existing client and business relationships between and among the professionals to a transaction (including but not limited to financial advisor, swap advisor, bond counsel, swap counsel, trustee, paying agent, underwriter, counterparty, and remarketing agent), as well as conduit issuers, sponsoring organizations and program administrators. This disclosure shall include that information reasonably sufficient to allow the Entity to appreciate the significance of the relationships.

Professionals who become involved in the debt transaction as a result of a bid submitted in a widely and publicly advertised competitive sale conducted using an industry standard, electronic bidding platform are not subject to this disclosure. No disclosure is required that would violate any rule or regulation of professional conduct.

## Appendix B

### Resources

1. **Government Finance Officers Association (GFOA)** ([www.gfoa.org](http://www.gfoa.org))
  - [Budgeting Best Practices](#)
  - [Debt Management Advisories](#)
  - [Debt Management Best Practices](#)
2. **International City/County Management Association** (<https://icma.org/>)
  - Management Policies in Local Government Finance, 6<sup>th</sup> Edition (<https://bookstore.icma.org/management-policies-in-local-government-finance-6th-edition-p43.aspx>)
3. **Municipal Technical Advisory Service** (<https://www.mtas.tennessee.edu>)
4. **County Technical Assistance Service** (<https://www.ctas.tennessee.edu>)
5. **Rating Agencies:**
  - [Fitch Ratings](#)
  - [Moody's](#)
  - [S&P Global Ratings](#)
6. **Municipal Securities Rulemaking Board** ([www.msrb.org](http://www.msrb.org))
  - [Electronic Municipal Market Access](#) (EMMA)
7. **Securities Industry and Financial Markets Association** ([www.sifma.org](http://www.sifma.org))
8. **California Debt and Investment Advisory Commission** ([www.treasurer.ca.gov/cdiac/](http://www.treasurer.ca.gov/cdiac/))

# Appendix C

## Glossary

**Conflicts of Interest** occur in situations where parties in a transaction have multiple interests or relationships that could possibly corrupt the motivation to act. The presence of a conflict of interest indicates the potential for divided loyalty and does not automatically indicate wrongdoing.

**Costs** are recurring and nonrecurring fees and expenses of professionals and service providers related to the issuance of debt, payable at the time the debt is incurred and/or during the life of the debt.

**Debt** is indebtedness lawfully issued, reissued, executed or assumed by a public entity. Debt is created when a public entity enters into an agreement to pay another entity in exchange for receiving an upfront payment or loan or for acquiring an asset. Common instruments or evidence of debt are:

**Bonds** are debt instruments issued for a period of one year or longer, usually for long-term financing.

**Notes** are debt instruments issued for a short period of time, often for interim financing. Examples are capital outlay notes, tax and revenue anticipation notes, bond anticipation notes, and grant anticipation notes.

**Financing Leases** are financial agreements where the lessor gives the lessee the right to use an asset in exchange for payment of funds and the agreement includes specific criteria that results in a debt obligation to the lessor.

**Loans** are financial agreements entered into by a public entity with a financial institution such as a local bank or a state or federal loan program. Examples may include but are not limited to State Revolving Fund Loan Programs or USDA Rural Development Loans.

**Debt Service** is a series of payments including interest (the true cost of borrowing paid to the obligor/investor) and principal (the amount of money borrowed or credit provided) required to be prepaid over a period of time. The rate of interest can be variable or fixed.

**Federal Compliance** is adherence to the federal rules, such as laws issued by the IRS related to the issuance of tax-exempt debt, or rules issued by the MSRB related to transparency and fair practices within the municipal securities market.

**Financial Transaction** is an agreement to exchange goods, services, or assets for payment.

## **Local Government is:**

**Tenn. Code Ann. § 9-22-133** – For the purposes of approval of balloon indebtedness, any incorporated city or town, metropolitan government, county, or utility district. It also includes any instrumentality of the aforementioned local governments.

**Tenn. Code Ann. § 9-21-409** – For the purposes of approval of debt with a variable rate, put option, and/or interest rate reset, any government issuing debt pursuant to the authority of Tenn. Code Ann., Title 9, Chapter 21.

**Professionals** are individuals or firms advising or providing professional services to a public entity with respect to a financial transaction. Examples of professionals are:

**Advisor** – an individual or firm with a deep knowledge in a specific area, engaged in the business of advising others. It can include a Financial, Swap, or Program Administrator.

**Counsel** – a legal advisor or attorney, whether an individual or a firm, representing a client. It can include Bond, Disclosure, Issuer, Swap, Tax, or Underwriters Counsel.

**Counterparty** – the entity on the opposite side of the transaction; usually it refers to the other party in an interest rate (or swap) agreement.

**Lender** – an individual or firm that provides funds to a borrower with the expectation that the funds will be repaid, usually with interest.

**Paying Agent** – an individual or firm that transfers the periodic interest and principal payments from the public entity to the investors.

**Registrar** – the individual or firm responsible for maintaining a record or list of owners or investors of the debt (sometimes referred to as holders of the debt).

**Remarketing Agent** – the firm responsible for reselling debt securities “tendered” by the current holders, to new investors. The remarketing agent is also usually responsible for resetting the interest rate for variable rate debt.

**Underwriter** – the firm that buys new debt for reselling to the public for a profit. The underwriter may acquire the debt either through negotiation or competitive bid.

**Verification Agent** – a certified public accountant or other independent third party that determines that the cash flow from investments purchased with proceeds of a refunding debt issue, along with other money, will be sufficient to pay the refunded bonds.



**Public Entity** is a governmental organization or unit that has a legal existence and is authorized to borrow money or enter into debt. It includes the State, state agencies, local governments, local government instrumentalities, and any other authority, board, district, instrumentality, or entity created by the State, a state agency, a local government, a local government instrumentality, or any combination of the above. It does not include legal entities without debt authority, such as a county school board; however, a special school district with debt authority is included.

**Governing Body** – the group of individuals with the authority to make decisions for a public entity, often referred to as the “legislative body.” Governing bodies are subject to the Tennessee Open Meetings Law (requiring public notice and recording of minutes). Members are the individuals serving on the governing body.

**Conduit Issuer** – a governmental entity or agency that issues debt for the purpose of lending the proceeds to another entity rather than financing a project for itself. Examples of conduit issuers are health and education boards, economic development boards, and public building authorities.

**Risk** refers to the uncertainty (downside) involved in a debt transaction, including investment, business, credit, market, liquidity, operations, tax, and basis risks.

**Security** is a term that is used both to describe a debt instrument that can be purchased, sold, or transferred to another party, or to describe property or an asset that is pledged as collateral to secure a debt.

**State Loan Programs** refer to programs offered by the state or state agencies. For example, the State Revolving Loan Program offered by the Tennessee Local Development Authority and the Energy Efficient Schools Initiative program offered by the State of Tennessee..

**State Funding Board** is the state entity whose members are the Governor, the Commissioner of Finance and Administration, the Comptroller, the State Treasurer, and the Secretary of State. The State Funding Board is created by Tenn. Code Ann. § 9-9-101.