

Debt Service

Debt Service is required to be reported in the budget certification statement to the Maryland State Department of Education under the Public School Laws of Maryland 1978, Chapter 22 of the Annotated Code of Maryland. Debt Service represents the periodic payments of principal and interest on bonded long and/or short-term indebtedness, and all costs associated with bond sales, issues, and cost to service debt.

Harford County Public Schools does not have the authority to issue such long term debt. The School system does have the authority to enter into alternative financing mechanisms such as leases and lease purchase transactions. The Harford County Government determines the long term debt financing levels to be used in conjunction with the Board of Education's Capital Improvements Program to be funded through the School Construction Fund. The County Treasurer's Office is responsible for administration of debt service, and the County Budget Office has graciously provided the following debt-related financial data. Before County General Funds are used to pay Board of Education Debt Service, the County utilizes Recordation taxes, Transfer taxes and school development impact fees. Both of these taxes were instituted to assist in debt payments and capital construction for the School's Capital Improvement Program.

The Recordation Tax was established by State law at the rate of \$4.40 per \$1,000 of actual consideration of debt secured as evidenced by documents recorded with the Clerk of the Circuit Court of Harford County. Receipts from this tax are dedicated to the repayment of debt service for school construction financing. In accordance with County Council Bill No. 93-3, the County established a one percent transfer tax. Fifty percent is dedicated to fund school site acquisition or school construction. The School Development Impact Fee was established by the County Government for all residential building permits applied for on or after July 1, 2005. The fees were established to assure that new development contributes its fair share towards the costs of public schools reasonably necessitated by such new development. The revised fees are imposed as of December 2009 and are \$6,000 for a single family detached home, \$4,200 for a townhouse/duplex and \$1,200 for all other residential dwellings including mobile homes.

County Government Debt Service on behalf of HCPS

Table 1¹

Debt Service Fund										
PRINCIPAL PAYMENTS	Actual FY 2012		Actual FY 2013		Actual FY 2014		Budget FY 2014		Projected FY 2015	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
School Bonds	\$15,020,096	91.7%	\$16,887,929	100.0%	\$17,533,083	100.0%	\$17,454,984	100.0%	\$18,497,996	100.0%
Short Term Notes	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%
Lease Purchase	\$1,360,707	8.3%	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%
TOTAL	\$16,380,803	100.0%	\$16,887,929	100.0%	\$17,533,083	100.0%	\$17,454,984	100.0%	\$18,497,996	100.0%
INTEREST PAYMENTS	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
	School Bonds	\$13,736,296	99.7%	\$12,848,886	100.0%	\$12,639,231	100.0%	\$13,173,669	100.0%	\$12,144,267
Short Term Notes	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%
Lease Purchase	\$38,543	0.3%	\$0	0.0%	\$0	0.0%	\$0	0.0%	\$0	0.0%
TOTAL	\$13,774,839	100.0%	\$12,848,886	100.0%	\$12,639,231	100.0%	\$13,173,669	100.0%	\$12,144,267	100.0%
SUMMARY	Actual FY 2012		Projected FY 2013		Projected FY 2013		Budget FY 2014		Projected FY 2015	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Principal	\$16,380,803	54.3%	\$16,887,929	56.8%	\$17,533,083	58.1%	\$17,454,984	57.0%	\$18,497,996	60.4%
Interest	\$13,774,839	45.7%	\$12,848,886	43.2%	\$12,639,231	41.9%	\$13,173,669	43.0%	\$12,144,267	39.6%
TOTAL	\$30,155,642	100.0%	\$29,736,815	100.0%	\$30,172,314	100.0%	\$30,628,653	100.0%	\$30,642,263	100.0%

¹ Data provided by Harford County Government.

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COUNTY PRACTICE

It is Harford County's practice to conduct a bi-annual bond sale contingent on capital project needs and the economic conditions of the bond market. Prior to selling bonds, the County will issue Bond Anticipation Notes (short term financing) or use existing cash flows to start the construction of capital projects based on cash flow needs.

On March 11, 2014, the County sold general obligation bonds of \$40,000,000 at a true interest cost of 3.046 percent. Including in this bond sale were Taxable Build America Bonds and Refunding Bonds. Revenues from the county sources of pay go funds, recordation taxes, transfer taxes, impact fees, and County general funds support the FY 2014 County debt service payments as outlined in the following chart:

*County Government Debt Service for HCPS
Table 2²*

Harford County, Maryland					
Budgeted FY 2015 County General Fund Principal and Interest Payments for Harford County Public Schools					
			PRINCIPAL	INTEREST	
SCHOOL BONDS:	2005	Bonds	\$1,354,911	\$101,618	
	2007	Bonds	\$3,894,630	\$716,248	
	2009	Refunding Bonds	\$882,563	\$113,198	
	2009	Bonds	\$3,688,666	\$3,079,198	
	2010	Refunding Bonds	\$1,192,702	\$394,698	
	2010 Series A	Bonds	\$5,448,600	\$1,861,605	
	2010 Series B	Bonds		\$3,203,777	
	2012	Refunding Bonds	\$513,428	\$117,160	
	2012	Bonds	\$706,605	\$418,576	
	2013	Bonds	\$507,992	\$375,474	
	2013	Refunding Bonds	\$114,841	\$1,611,639	
	2014	Bonds	\$193,058	\$151,076	
	TOTAL SCHOOL BONDS			\$18,497,996	\$12,144,267

While Debt Service Table 1 indicates the specific amounts of bonded indebtedness undertaken by Harford County Government for the Board of Education in FY 2005 through FY 2014, the following information is provided to clarify the fiscal policies of Harford County, which is responsible, for issuing, managing, and retiring debt obligations associated with Harford County Public Schools. The Board of Education has no authority to issue long term debt such as General Obligation Bonds.

Debt management is an important component of a county's financial management practices. Governments use the option of debt financing to pay for large projects, such as schools, when paying for governmental activities with roads, schools, libraries, and public buildings being the more common uses of bond proceeds.

Debt management is important to ensure that:

- The amount of debt issued by the County is affordable given the County's anticipated revenue levels and operating needs;
- The County issues the kinds of debt appropriate to given projects at the lowest possible interest cost; and,
- The County issues debt in compliance with all relevant laws and regulations.

Section 524 of the Harford County Charter states that the County may incur debt. Furthermore, no indebtedness for a term of one year or greater shall be incurred by the County to meet current operating expenses. All County indebtedness for a term in excess of one year shall become due no later than 30 years after the date of issuance, except debt incurred to finance water, sewer and wastewater facilities, which shall become due no later than 40 years after the date of issuance.

² Data contained in Harford County Government Approved FY 2015 Capital Budget, page 85.

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LONG-TERM FINANCING TECHNIQUES

General Obligation Bonds – General Obligations Bonds are known as full faith and credit bonds since their payment is based on the general credit and taxing power of the County. The quality of the general obligation bonds is derived from the fiscal and economic strengths of the County and its ability to assure repayment of monies borrowed. General Obligation Bonds, being tax-supported, are typically used to finance the capital portion of tax supported general public purpose capital projects.

Lease Purchase/Certificates of Participation – Obligations of a public entity secured by an installment sale or leaseback arrangement with a public entity lease. The lessee generally pledges general operating revenues to pay the lease payments, which may or may not be reimbursed by revenues from the project. These obligations do not constitute indebtedness under state constitutional debt limitation. Payment to be made under valid leases are payable only in the year in which use and occupancy of the leased property is available, and lease payments may not be accelerated.

BOND RATINGS

The County's General Obligation AAA bond rating by Moody's Investors Service, Standard and Poor's, and Fitch reflect the County's strong credit rating. All three rating services awarded AAA status to Harford County in March 2014. Credit ratings are designations by the investor's services to give a relative indication of credit quality, with Aaa/AAA/AAA being the highest achievable rating. Factors contributing to the County's relative high ratings include historically strong financial performance, along with tax raising flexibility, a low debt profile, and ongoing growth and diversification in the economic base.

Bond Ratings on March 11, 2014:

- Fitch Ratings AAA
- Moody's Investors Aaa
- Standard & Poor's AAA

DEBT MANAGEMENT

Traditionally, Harford County sold bonds only for construction of capital projects within the Capital Improvement Program during the period of 1948 through 1982. Projects must have legislative approval before engineering or construction contracts can be awarded. A pay-as-you-go (PAYGO) policy was implemented in July 1984 for funding capital projects for the general county, education, fire, library, college, highways, and certain water and sewer projects.

In order to provide an adequate physical infrastructure, improved services, and channel growth while maintaining the County's quality of life, a more balanced approach to capital funding has been adopted. Projects within the General Capital Program will be financed with PAYGO funding when feasible rather than long term debt. The County has established a policy where they will keep bonded debt and its resulting debt service to as small a portion of the General Fund Budget as is realistically possible, while not tied to a set ratio. The County will hold conservative, yet fluid and responsive, debt management to be fiscally prudent.

*County Government Legal Debt Margin
Table 3³*

Statement of Legal Debt Margin as of June 30, 2013		
Debt Margin Calculation	Bonded Debt	Debt Limit
Legal Debt Limit		\$1,714,305,453
Amount of Debt applicable to Debt Limit	\$660,169,543	
Less:		
Self-sustaining Debt:	(207,574,381)	
Total Amount of Debt Applicable to Debt Limit		<u>452,595,162</u>
Legal Debt Margin		\$1,261,710,291

³ Debt Service data is from Harford County Government Comprehensive Annual Financial Report for the year ended June 30, 2013, page 138.

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DEBT LIMITATIONS

According to state law⁴, the County, as a charter county, is limited in the amount of general obligation supported debt that it can issue to an amount equal to a total of 6 percent of the assessable value of real property of the County and 15 percent of the assessed value of the personal property and operating real property in the County. As of June 30, 2013, the estimated debt limit of the County is \$1,714,305,453.

The County's estimated outstanding general obligation supported debt as of June 30, 2013, exclusive of self-supporting/self-liquidating debt not applicable to the debt limit, is \$452,595,162. This allows for an excess of allowable debt over outstanding non-self-liquidating debt of \$1,261,710,291 as calculated in Debt Service Table 3.

Debt Service Table 4⁵

Harford County Government Statement of Direct and Overlapping Debt as of June 30, 2013		
General Obligation Debt	\$660,169,543	
Self-Liquidating Debt Outstanding		
Water and Sewer Bonds	(\$61,104,712)	
Tax Incentive Finance Fund	(\$14,000,000)	
Special Revenue Fund Bonds	(\$132,469,669)	
Total Direct Debt		\$452,595,162
Overlapping Debt:		
City of Aberdeen	\$5,004,101	
Town of Bel Air	\$2,745,768	
City of Havre de Grace	\$28,601,369	
Total Overlapping Debt		\$36,351,238
Total Direct and Overlapping Debt		\$488,946,400

DEBT BURDEN

Debt burden is a measurement of the relationship between the debt of the County supported as a percentage of personal income and population. The broadest and most generally available measure of wealth in the community is debt as a percentage of personal income. In addition, debt can be compared to population to determine a per capita burden level.

The County makes these comparisons each time it offers bonds for sale. They are included in the official statements that are distributed to prospective investors. Additional ratio comparisons are provided to help understand the debt load in Debt Service Tables 4 and 5.

⁴Annotated Code of Maryland, Article 25A, §5(P)

⁵ Debt Service data is from Harford County Government Comprehensive Annual Financial Report for the year ended June 30, 2013, page 138 & 139.

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County Government Debt Service Table 5⁶

Debt Ratios FY 2009 to 2013

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Ratio of Debt to Personal Income	4.30%	5.53%	5.31%	5.31%	5.15%
Ratio of Debt per Capita	\$1,964	\$2,590	\$2,619	\$2,669	\$2,667

BUSINESS PLAN

In order to help understand the framework used by the County government in establishing funding for Harford County Public Schools, it is useful to become familiar with the Harford County Government's Business Plan. Under the

Plan, the annual budget is to be adjusted as a result of economic conditions in the County, state, and nation. Capital projects may progress more rapidly or more slowly depending on population growth, economic, and funding sources.

The County has developed a business model for capital project funding for the current and the next succeeding five fiscal years. The model sets the following goals:

1. Expenditures will be reviewed and approved based on real versus perceived need;
2. Each function, service, project, and expenditure as to its affordability;
3. New sources of revenue will be identified and advanced;
4. Prepare, integrate through planning, and maintain conservative annual operating budgets and multi-year spending plans;
5. Plan for and preserve a prescribed year-end fund balance to maintain the credit rating and provide for emergency needs; and,
6. Develop and implement a new five year capital program based on affordability and sound debt management practices.

Pay-as-you-go (PAYGO) funding will continue to be used for minor renovation and repair projects which have an asset life of less than ten years. The PAYGO policy has allowed the County to plan more efficiently how annual budgets and capital improvements programs will be undertaken while maintaining the same property tax rate.

The General County Capital Program includes general government, education, police/sheriff/fire, community college, libraries, highway, landfill, and parks and recreation projects. Lease-purchase financing of capital assets will be analyzed and assessed as an alternative to long-term bond financing. Utility capital projects will be financed with long-term debt, only after funding sources have been established to pay the annual debt payments, such as PAYGO funding and/or assessments to property owners who will benefit from the improvements.

The County has issued a combination of debt⁷ (general obligation bonds, lease purchase agreements) in financing capital projects for the school system. The July 1, 2013 outstanding balance of debt issued for the school system projects was \$287,588,281: principal and interest payments during FY 2014 were \$17,533,082. Additional debt was

Issued on behalf of the school system in fiscal year 2014 of \$3,860,234. The outstanding balance of debt at June 30, 2014 was \$273,915,433.

⁶ Debt Service data is from Harford County Government Comprehensive Annual Financial Report for the year ended June 30, 2013, page 137.

⁷ Debt data is the most current information from Harford County Government, Treasury Department for the year ended June 30, 2014.

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HARFORD COUNTY PUBLIC SCHOOLS DEBT SERVICE

Harford County Public Schools does not have the authority to issue long term debt. The School System does have the authority to enter into alternative financing mechanisms such as leases and lease purchase transactions. The School System entered into energy performance construction contracts in 2001 and 2002, which were financed with equipment lease purchase transactions. Both transactions had a fifteen year term. The School System entered into a lease purchase for the construction of a new administration building in September 2004 for a 25 year term.

Due to favorable interest rates, in early 2012 the energy performance and administrative building leases were refinanced over the remaining life of the original leases. The original interest rates for the administration building (5.0%), energy performance phase I (5.0%) and energy performance phase II (4.3%) were refinanced at lower interest rates of 3.3%, 1.9% and 2.0% respectively.

In addition, the school system has completed negotiations for an additional energy performance lease in the amount of \$14,248,426 with an annual interest rate of 2.1%. The energy lease phase three will be funded beginning in fiscal year 2014 and ending in fiscal year 2030. These Transactions were approved by the County Executive and County Council. Payments are included in the Unrestricted Funds Budget and are identified in Table 6.

Debt Service Table 6⁸

Harford County Public Schools Debt Service Fund					
PRINCIPAL PAYMENTS	Actual FY 2012	Actual FY 2013	Actual FY 2014	Budget FY 2014	Budget FY 2015
SunTrust Lease Energy Phase I - A	\$265,025	\$214,364	\$367,191	\$367,191	\$374,160
SunTrust Lease Energy Phase II - B	\$305,287	\$377,058	\$404,418	\$404,418	\$412,395
SunTrust Lease Energy Phase III - C		\$0		\$0	\$0
US Bank Administration Bldg - D	\$327,235	\$0		\$0	\$371,258
TOTAL	\$897,547	\$591,422	\$771,609	\$771,609	\$1,157,813
INTEREST PAYMENTS					
SunTrust Lease Energy Phase I - A	\$101,631	\$31,723	\$28,734	\$28,734	\$21,835
SunTrust Lease Energy Phase II - B	\$122,502	\$46,661	\$41,657	\$41,657	\$33,610
SunTrust Lease Energy Phase III - C			\$297,769	\$297,769	\$287,390
US Bank Administration Bldg - D	\$496,587	\$246,568	\$327,544	\$327,544	\$327,544
TOTAL	\$720,720	\$324,952	\$695,704	\$695,704	\$670,379
SUMMARY	Actual FY 2012	Actual FY 2013	Actual FY 2014	Budget FY 2014	Budget FY 2015
Principal	\$897,547	\$591,422	\$771,609	\$771,609	\$1,157,813
Interest	\$720,720	\$324,952	\$695,704	\$695,704	\$670,379
TOTAL	\$1,618,267	\$916,374	\$1,467,313	\$1,467,313	\$1,828,192

A - SunTrust Lease dated December 7, 2001 was refunded June 19, 2012

B - SunTrust Lease dated December 19, 2002 was refunded June 19, 2012

C- JP Morgan Lease dated December 19, 2012

D- SunTrust Lease dated September 1, 2004 was refunded May 30, 2012

⁸ Data is from Harford County Public Schools Budget Office.