DEBT FINANCING TERMS AND CONCEPTS

This appendix is designed to provide definitions for terms and concepts used in connection with debt issuance. To be consistent with customary industry practice, the term bonds is used to mean either long-term bonds or, more generally, bonds, notes, commercial paper, and other types of evidence of debt.

ACCRUED INTEREST

In general, interest that has been earned on a bond but not yet paid—usually because it is not yet due.

AD VALOREM TAXES

An annual tax that is a uniform percentage of the value (or assessed value) of property.

ADVANCE REFUNDING

See Refunding.

AMORTIZE

To retire the principal of an issue by periodic payments either directly to bondholders, or first to a sinking fund and then to bondholders.

ARBITRAGE YIELD RESTRICTION

With respect to municipal bonds, arbitrage is the profit made by issuing bonds bearing interest at tax-exempt rates, and investing the proceeds at materially higher taxable yields.

ASSESSMENTS

Assessments are charges in the nature of taxes upon property owners to pay the costs of facilities or improvements that benefit the property.

BOND INSURANCE

Noncancellable insurance purchased by the issuer from a bond insurer pursuant to which the insurer promises to make scheduled payments of interest, principal, and mandatory sinking fund payments on an issue if the issuer fails to make timely payments.

Bond insurance is never a substitute for the underlying creditworthiness of the issuer.
CALL
To give notice of redemption; to redeem.

CAPITALIZED INTEREST (FUNDED INTEREST)
Bond proceeds reserved to pay interest on an issue for a period of time early in the term of the issue—also called funded interest. Capitalized interest may also refer to the interest to be so paid.

To give notice of redemption; to redeem. Commonly, in a project financing, interest is capitalized through the date on which it is anticipated that construction of the project being financed with the proceeds will be completed and the date when the project will be operating and capable of providing revenues for repayment of debt service.

CASH FLOW
A comparison of cash receipts (revenues) to required payments (generally, debt service and operating expenses).

A cash flow may demonstrate that receipts by an issuer from a project’s revenues or a mortgage portfolio, or from collection of a tax, fee, or other charge will be sufficient to equal or exceed, in each year the sum of payments of principal and interest on an issue and related expenses, generally on the basis of specified assumptions, which may include a “worst case” scenario.

COMMERCIAL PAPER
Notes varying very short-term maturities (generally one to two hundred and seventy days), which are intended to be rolled over in a series of current refundings as portions of the issue mature from time to time.

Generally, the maturity of the commercial paper sold on each rollover is determined by market conditions at the time of rollover

COMPETITIVE SALE
The sale of bonds to the bidder presenting the best sealed bid at the time and place specified in a published notice of sale.

When bonds are to be sold at a competitive sale, the issuer typically specifies all the terms of the issue other than interest rates and purchase price. When the issue is ready to market, the issuer solicits bids by placing a notice of sale in one or more industry publications such as The Wall Street Journal or The Bond Buyer and, if required by law, in a local newspaper of general circulation. In the notice of sale, the issuer announces that it will accept sealed bids until a certain date and time. Prior to presenting bids the underwriters evaluate the credit quality of the issue and the municipal market and may form syndicates or selling groups. The bonds are awarded to the underwriters presenting the best bid based on the criteria specified in the notice of sale.
COMPUND

To treat accrued interest as if it were principal, so that interest thereafter accrues on the sum of the principal and the compounded interest.

COMPOUND INTEREST BOND

A bond on which interest is not payable until maturity (or earlier redemption), but compounds periodically to accumulate to a stated maturity amount.

These bonds are also called capital appreciation bonds or CABs and are sometimes misnamed zero coupon bonds.

COSTS OF ISSUANCE

Costs of issuance are the expenses paid by or on behalf of the issuer in connection with the sale and issuance of bonds.

These expenses may include, but are not limited to, bond counsel's fees, disclosure counsel fees, trustee's fees, financial advisor's fees, feasibility consultant's fees, accounting fees, costs of printing the bonds, costs of printing the Official Statement or other disclosure documents, costs associated with obtaining a credit rating, and underwriter's gross spread. For some types of bonds the costs of issuance can be paid from the proceeds.

COUPON BOND

A bond that generally has a number of interest coupons attached to it and which is transferable merely by delivering it to its new owner.

COVENANTS

Contractual obligations in financing agreements whereby the party making the promises agrees to perform or refrain from performing certain actions or to comply with certain requirements.

Most issuer covenants are found in the indenture or bond resolution pursuant to which the bonds are issued. However, in a conduit financing, the covenants of the nongovernmental borrower are often set forth in a loan agreement.

CUSIP

The acronym for Committee on Uniform Security Identification Procedures, which was established under the auspices of the American Bankers Association to develop a uniform method of identifying municipal, United States government, and corporate securities.

A separate CUSIP number is assigned for each maturity of each issue and is printed on each bond.
**DATE OF ISSUANCE/ORIGINAL ISSUANCE DATE**

The date of issuance is the same as the closing date. However, the original issuance date, as used on the standard registered bond form, is the same as the dated date.

**DEBT LIMIT**

A statutory or constitutional limit on the amount of debt that an issuer may incur or that it may have outstanding at any one time.

**DEBT SERVICE**

The total of interest, principal, and mandatory sinking fund payments.

**DEBT SERVICE ACCOUNT**

The account or accounts into which the issuer makes periodic deposits to assure the timely availability of sufficient monies for the payment of debt service on an issue.

**DEFAULT/EVENT OF DEFAULT**

Failure to make prompt payment on a bond or otherwise comply with other covenants in the financing agreements.

Indentures and bond resolutions commonly provide for some short period of time—a cure period—to correct a failure to comply with a covenant before a simple default becomes an event of default that allows acceleration and certain other remedies to be pursued.

**DEFEASANCE**

The termination of the rights and interests (including the pledge of revenues but not including the right to payment) of the bondholders under the indenture or bond resolution upon final payment or provision for payment of all debt service on the bonds, all in the specific manner required by the indenture or bond resolution.

In an advance refunding, the defeasance of the bonds being refunded is generally accomplished by placing in an escrow sufficient high quality investments to provide for payment of debt service on the bonds to redemption or maturity.

**DEMAND BOND (PUT BOND OR TENDER OPTION BOND)**

A bond that the holder has the right to sell back to the issuer, a nongovernmental borrower, or another party at specified times and for a specified price (usually par).

Variable rate bonds generally have a demand feature. The demand feature gives the holder investment flexibility and protection against fluctuating market interest rates and other risks. The interest rate rises or falls in step with market rates, and the holder has the option to keep the bond or to demand the purchase of the bond in accordance with the holder's investment needs.
Demand bonds are sometimes referred to as put bonds or tender option bonds because the holder can “put,” or has an option to tender, the bond back to the issuer.

Put bonds that are tendered are customarily remarketed. If not, they may be purchased using monies available for that purpose, including advances under a line of credit or draws under a letter of credit.

**DENOMINATION**

The face amount of a bond—generally its original principal amount. Usually the denominations are $5,000 or any integral multiple of $5,000. In some short-term or variable rate financings, denominations may be multiples of $100,000 or in multiples of $5,000 in excess of $100,000.

**DISCLOSURE**

Providing to investors (usually in the form of an Official Statement) all material facts relating to an issue.

**DISCOUNT**

The amount, if any, by which the principal amount or par value of a bond exceeds its sale price.

**DUE DILIGENCE**

The inquiry made to reveal or confirm facts about the issuer, the issue, and the security for the issue that would be material to a prudent investor in making a decision to purchase the issue.

**ESCROW AGENT**

With respect to an advance refunding, the commercial bank or trust company retained to hold the investments purchased with the proceeds of the refunding and, customarily, to use the amounts received as payments on such investments to pay debt service on the refunded bonds.

**FISCAL AGENT**

A commercial bank or trust company designated by an issuer under the indenture or bond resolution to act as a fiduciary and as the custodian of monies relating to an issue.

The fiscal agent’s duties typically are limited to receiving monies from the issuer that are to be held in funds and accounts created under the indenture or bond resolution and, when acting as paying agent, paying out principal and interest to bondholders.

**FIXED RATE**

An interest rate that is set at the time a bond is issued and that does not vary during the term of the bond.
GOOD FAITH DEPOSIT

A deposit made by an underwriter with the issuer of a new issue as assurance that the underwriter will proceed with the closing of the purchase of the issue if the issuer meets all of the conditions of the bond purchase contract.

INDENTURE/BOND RESOLUTION (GENERAL, SUPPLEMENTAL, AND SERIES)

An agreement executed by an issuer and a trustee (or fiscal agent) that pledges certain revenues and other property as security for the repayment of the issue, sets forth the terms of the bonds, and contains the responsibilities and duties of the trustee and the rights of the bondholders.

The responsibilities and duties of the trustee may include, among others, the following:

- Regulating the disbursement of proceeds of the issue for the intended purpose
- Funding transfers to assure that bondholders receive timely and complete payment
- Protecting the assets of the trust if a default occurs, and
- Exercising a specified standard of care in the administration of those trusts

The rights of bondholders are set forth in indenture provisions relating to the timing of interest and principal payments, interest rate setting mechanisms (in the case of variable rate bonds), redemption provisions, events of default, remedies, and the mailing of notices of various events. The indenture typically also contains the text to be printed on the bond.

INTEREST/INTEREST RATE

A charge paid to the bondholder by the issuer for the use or borrowing of money. The interest rate is the interest charge expressed as a percentage of principal (which generally corresponds roughly to the amount borrowed) accruing over a specified period (generally a year) so long as the debt remains unpaid.

INVESTMENT OF PROCEEDS

The investment of proceeds and other monies relating to an issue is typically governed by state law and by the indenture or bond resolution.

Either document may prescribe both the types of investments that may be purchased (e.g. U.S. Treasury obligations, bank certificates of deposit, or corporate obligations with a specified rating) and the maximum maturity of investments of certain funds (e.g. short-term investments for monies to be used to make the next debt service payment or longer term investments for reserves). The arbitrage rules under federal tax law may regulate the yield at which proceeds may be invested and may require rebate of certain investment earnings.
**ISSUE**

One or more bonds initially delivered by an issuer in a substantially simultaneous transaction and which are generally designated in a manner that distinguishes them from bonds of other issues.

**LETTER OF CREDIT**

An arrangement with a bank that provides additional security that money will be available to pay debt service on an issue.

**LINE OF CREDIT**

A line of credit is a contract between the issuer and a bank that provides a source of borrowed monies to the issuer in the event that monies available to pay debt service (e.g. on commercial paper) or to purchase a demand bond are insufficient for that purpose.

**LIQUIDITY**

The ease with which an investment may be converted to cash, either by selling it in the secondary market or by demanding its repurchase pursuant to a put or other prearranged agreement with the issuer or another party.

**MATERIAL/MATERIAL FACTS**

Facts that a reasonably prudent investor would want to know in making an investment decision.

**MATURE**

With respect to a single bond, the date upon which the principal of the bond is stated to be due. With respect to an issue, all of the bonds of an issue that are due on a single date.

**MUNICIPAL SECURITIES RULEMAKING BOARD (MSRB)**

An independent, self-regulatory organization established by Congress in 1975 having general rulemaking authority over municipal securities market participants (generally, brokers and dealers).

The MSRB is required by federal law to propose and adopt rules in the areas of professional qualification standards, rules of fair practice, record keeping, the scope and frequency of compliance examinations, the form and content of municipal bond quotations, and sales to related portfolios during the underwriting period.

The 15 MSRB members include 5 from each of 3 categories—securities firms’ representatives, bank dealer representatives, and public members. All market participants subject to MSRB jurisdiction are required to register with the SEC. Its jurisdiction does not extend to issuers of municipal securities. In recognition of the existing regulatory structure in place for banks and securities firms, the MSRB does not have inspection or enforcement authority.
**Negotiated Sale**

A sale of bonds, the terms and price of which are negotiated by the issuer through an exclusive agreement with a previously selected underwriter and/or underwriting syndicate. Unlike a competitive sale, the underwriter is customarily active in all aspects of structuring the negotiated deal. Selection of the underwriter can be based on many different considerations including, but not limited to, expertise with a particular type of issue, market expertise, reputation, guaranties of maintaining a maximum gross spread, as well as prior relationships with the issuer.

**Net Interest Cost (NIC)**

A measure of the interest cost of an issue derived by adding together all interest payments for the term of the issue and dividing that sum by the sum for all bonds of the amount of each bond multiplied by the number of years it is outstanding.

**Notice of Sale**

The document that issuers use to solicit bids from prospective underwriters for a competitive sale of bonds.

The notice will commonly be published in a financial industry journal, usually *The Bond Buyer* or *The Wall Street Journal* (and, if required by law, a local newspaper of general circulation) and will list the details concerning an issue. This may include:

- The date, time and place of the sale
- The amount of the issue, maturity schedule, and redemption provisions
- Legal authority for the sale
- The manner in which the bid is to be delivered
- The type of security (general obligation, pledge of revenues, etc.)
- Limitations on interest rates and interest payment dates
- Denominations and registration provisions (registered, book entry, etc.)
- Names of bond counsel and any other attorneys delivering opinions, credit enhancement facilities, and other details
- The notice of sale, the winning bid and the issuer's acceptance of the winning bid together constitute an agreement for the purchase and sale of the issue in a competitive sale.

**Official Statement/Preliminary Official Statement**

A document containing information about the bonds being offered, the issuer, and the sources of repayment of the bonds.
Federal securities laws generally require that if an Official Statement is used to market an issue, it must fully disclose all facts that would be of interest (i.e. material) to a potential buyer of bonds of the issue. For example, for a general obligation issue, the most important information may concern the financial health of the issuer, its tax base, and the economic health of the jurisdiction. For a water revenue issue, the most important information may be the financial health and physical condition of the water system enterprise, water supply, and the economic health of the service area. For a conduit financing, the most important information may concern the financial health of the nongovernmental borrower. The materiality of such information may also depend upon whether or not credit enhancement is utilized.

Under MSRB rules, a final Official Statement—which is printed only after the final terms of the bonds are available—must (if available) be delivered by the broker or dealer to purchasers of bonds no later than the settlement date of the transaction. An Official Statement may also be called an Offering Circular, Offering Memorandum, or bond prospectus.

**OUTSTANDING**

In general, as used with respect to the principal of an issue, the amount remaining unpaid.

However, the terms of indentures and bond resolutions often provide that bonds, which are not yet paid but are the subject of a defeasance or an advance refunding, are treated as no longer being outstanding.

**PAR/PAR VALUE**

Par or par value refers to the principal amount of a bond.

A bond may be purchased at par—meaning the price of the bond is equal to its principal amount, below par—meaning the price is below its principal amount, or above par—meaning the price is above its principal amount.

**PAYING AGENT**

The institution—usually a commercial bank or trust company—appointed in the indenture or bond resolution to act as the agent of the issuer to pay principal and interest from monies provided by or on behalf of the issuer.

**PREMIUM**

The amount by which the price of a bond exceeds its principal amount or par value.

**PRICING/REPRICING**

The determination (or redetermination) by the underwriters in a negotiated sale of the interest rates and reoffering prices at which an issue will be offered to investors.
Generally, the underwriters will have mailed a Preliminary Official Statement to potential investors and to other underwriters approximately one to two weeks prior to the pricing date. On the pricing date the underwriters will price the issue at the lowest marketable interest cost to the issuer. The price must be agreeable to the issuer. The underwriters then offer the bonds to investors on the agreed terms and if an appropriate number of orders are received, the issuer and the underwriters enter into a bond purchase contract on those terms. If not enough or too many orders are received on the original terms, the issue may be repriced to be more attractive to investors or to give a better rate to the issuer, as the case may be.

**PRIVATE PLACEMENT**

The offer and sale of an issue by the issuer directly to one or more investors, rather than through an underwriter.

Often, the terms of the issue are negotiated directly between the issuer and the investor. Sometimes, an investment banker will act as placement agent, bringing the parties together and acting as an intermediary in the negotiations. Instead of an Official Statement, an Offering Circular, Offering Memorandum, or Private Placement Memorandum may be prepared.

**PROCEEDS/SALE PROCEEDS/INVESTMENT PROCEEDS/GROSS PROCEEDS/NET PROCEEDS**

Proceeds are comprised of sale proceeds and investment proceeds. Sale proceeds are the amount paid by the ultimate purchasers (not including an underwriter) of a new issue, excluding any accrued interest.

The term gross proceeds refers to all of the monies relating to an issue, which are subject to arbitrage limitations and rebate under the Tax Code. Gross proceeds include sale proceeds, investment proceeds, and any other monies pledged to pay debt service and expected to be used to pay debt service, including monies in a sinking fund and monies in a reserve account.

The term net proceeds refers to all proceeds less any investment proceeds earned after completion of the financed project.

**PROJECT FINANCING**

An issue for the purpose of financing all or a portion of the costs of acquiring, constructing, and/or renovating a specified project for a public or private entity.

**PUBLIC OFFERING**

The sale of bonds (generally through an underwriter) to the general public (or a limited section of the general public).
**REBATE REQUIREMENT**

To pay to the U.S. government (or in the case of certain qualified single-family mortgage revenue bonds, to mortgagors) amounts earned from the investment of gross proceeds at a yield in excess of the yield on the issue.

**REDEMPTION**

The payment of principal of a bond, whether at maturity, or—under certain circumstances described in the bond—prior to maturity. Redemption of a bond by the issuer prior to maturity is sometimes referred to as calling the bond. Redemption prior to maturity may be optional, mandatory, or extraordinary (sometimes also called special).

**REFUNDING**

An issue of new bonds (the refunding bonds) to pay debt service on a prior issue (the refunded bonds).

Generally, the purpose of a refunding is either to reduce the debt service on the financing or to remove or replace a restrictive covenant imposed by the terms of the refunded bonds (for example, an excessive coverage ratio).

The proceeds of the refunding bonds are either deposited in escrow to pay the refunded bonds when subsequently due or applied immediately to the payment of the refunded bonds.

**Advance Refunding**

A refunding in which the refunding bonds are issued more than 90 days prior to (in advance of) the date upon which the refunded bonds will be repaid.

**Current Refunding**

A refunding in which refunding bonds are issued not more than 90 days before the date upon which the refunded bonds will be paid.

**REGISTERED BOND**

A bond for which the name and address of the legal owner is required to be listed on the bond registration books of the trustee or a registrar.

Generally, interest payments on a registered bond are made by check or wire sent to the registered owner. The registered owner may not be the beneficial owner of the bond, but rather a nominee for the beneficial owner. If the registered owner is a broker/dealer acting as nominee for a client, the bond is referred to as being held in “street name.” Registered bonds are often held in the name of a securities depository or in the name of a nominee for a securities depository, such as Depository Trust Company, which then keeps a record of the broker/dealers whose clients are the beneficial owners of the bonds.
REGISTRAR

The agent of the issuer appointed to maintain a list of the names and addresses of all registered owners of the bonds and to record transfers and exchanges of the bonds.

REMARKET

To buy and resell to the public previously issued bonds that have been or are required to be purchased from the original or subsequent holders of the bonds by the issuer or another party upon the occurrence of certain events specified in the legal documents.

REMARKETING AGENT

The investment bank or commercial bank retained to remarket bonds that have been tendered for purchase by the issuer or another party pursuant to an option to sell (a put) that accompanies the bond.

RESERVE ACCOUNT (BOND RESERVE ACCOUNT OR DEBT SERVICE RESERVE ACCOUNT)

An account from which monies may be drawn to pay debt service on an issue if pledged revenues and other amounts available to satisfy debt service are temporarily insufficient.

SEC REGISTRATION

The filing of information with the SEC in accordance with the Securities Act of 1933 as a prerequisite to selling or marketing securities.

Most bonds issued by or on behalf of state or local governmental entities are exempt from such registration requirements.

SEC RULE 15c2-12

A rule promulgated by the SEC under the Securities Exchange Act of 1934 concerning disclosure and continuing disclosure requirements for municipal securities.

SECONDARY MARKET

The market in which bonds are purchased from bondholders who have held such bonds for investment purposes, as opposed to being purchased directly from the issuer or from the issuer through an underwriter.

SERIAL BONDS

Bonds of an issue, which are payable as to principal in amounts due at successive regular intervals, generally annual or semiannual and usually in the early years of the term of the issue. An issue may consist of both serial bonds and term bonds. Generally, sinking fund payments are mandatory in a specified amount for each payment period to provide for the periodic redemption of term bonds prior to their final maturity.
SLGS

An acronym (pronounced “slugs”) for a type of U.S. Treasury obligation, the complete name of which is United States Treasury Securities - State and Local Government Series.

SLGS are an investment vehicle made available by the U.S. Bureau of Public Debt for investment of gross proceeds. The Bureau of Public Debt offers three types of SLGS, which are commonly referred to as Demand Deposit SLGS, Time Deposit SLGS, and Zero SLGS. Generally, Time Deposit SLGS are acquired in connection with an advance refunding. The SLGS are held in escrow, and principal and interest received on the SLGS are used to pay debt service on the prior issue. Because the issuer can specify the rate (subject to the maximum rate specified in a weekly schedule) earned on the SLGS, the issuer may design the escrow investment to meet any yield restrictions while maximizing its permitted investment return. Demand Deposit SLGS are intended for the investment of monies subject to the rebate requirements. Earnings on Demand Deposit SLGS are not subject to the rebate requirement. The interest rate on the Demand Deposit SLGS is determined weekly, effective each Monday and is calculated based upon a formula which takes into account the Federal Funds Rate which is published by the Federal Reserve Board and an estimated average marginal tax rate of owners of short-term municipal securities and an administrative fee. The estimated marginal tax rate and the administrative fee may be changed periodically by the Bureau of Public Debt. Zero SLGS bear interest at 0 percent, have flexible purchase and redemption terms, and are designed to be used to average down investment yields on open market securities for yield restriction purposes.

TERM

With respect to a single bond, the period of time until the maturity date of the bond and with respect to an issue, the period until the maturity date of the last bond of the issue to mature.

TERM BONDS

Originally, the maturity due at the end of the term of an issue; now, more commonly, a maturity that is subject to redemption over a specified period from sinking fund payments.

VARIABLE RATE

An interest rate that periodically changes based upon an index or a pricing procedure.

YIELD CURVE

Yield curve means the curve obtained by plotting the yield of investment or debt instruments (on the x-axis) against time (on the y-axis). The typical yield curve is upward sloping, so that the shorter the maturity of the instrument, the lower the yield of that instrument. However, this is not always true, and sometimes yield curves flatten out or even become inverted. The yield curve varies over time in response to general economic conditions and the yield curve may be differently sloped for different types of instruments depending on credit quality, tax-exempt status, and other factors.