DEBT MANAGEMENT POLICY

I. Statement of Purpose

The purpose of the Fredericksburg Independent School District Debt Management Policy (the "Policy") is to establish and maintain well defined debt management guidelines for issuing new debt as well as managing outstanding debt to sustain a strong debt management program.

II. Scope

The Policy applies to all debt instruments issued by the District regardless of the purpose for which issued or the funding source for repayment.

III. Objective

The primary objective is to ensure prudent debt management practices which:

A. Maintain financial stability;
B. Preserve public trust;
C. Minimize costs to taxpayers;
D. Minimize borrowing costs;
E. Preserve access to financial markets; and
F. Maintain and improve the District's credit rating.

IV. Types of Authorized Debt - The District is authorized to issue the following types of debt as approved by the Texas Education Code and the Texas Government Code:

A. Unlimited Tax Bonds - The Texas Education Code § 45.001 authorizes school districts to issue bonds for the construction, acquisition, and equipment of school buildings, the purchase of necessary sites for school buildings, and the purchase of new school buses. The District secures these bonds through levying, pledging, assessing and collecting annual ad valorem taxes, without limit as to rate or amount, sufficient to pay the principal and interest on the bonds as they become due. The bonds must mature serially or otherwise not more than 40 years from their issuance date and may be redeemable before maturity. The bonds require voter approval to be issued (§ 45.003(a)) and may be sold at a public or private sale.

B. Maintenance Tax Notes and Tax Anticipation Notes - The District may pledge any available funds of the District, including the proceeds of its maintenance tax, to secure negotiable maintenance tax notes and tax anticipation notes under § 45.108 of the Texas Education Code. The proceeds of these notes may be used for any legal maintenance expenditure including environmental clean-up and asbestos removal programs or maintenance, repair, rehabilitation, or replacement of heating, air conditioning, water, sanitation, roofing, flooring, electric or other building systems of existing school properties. Notes issued pursuant to this section may not at any time exceed 75 percent of the previous year's income, may be issued only after a budget has been adopted for the current school year, and must mature not more than 20 years from their date.

C. Delinquent Tax Notes - § 45.104 of the Texas Education Code authorizes the District to pledge any delinquent taxes levied for maintenance purposes to secure a loan and may evidence such loan with negotiable notes. The proceeds of these loans may be employed for any legal maintenance expenditure including all costs incurred in connection with environmental clean-up and asbestos removal programs or maintenance, repair, rehabilitation or replacement of heating, air conditioning, water, sanitation, roofing, flooring, electric or other building systems of existing school properties. Negotiable notes issued under this section must mature not more than 20 years from their date.

D. Time Warrants - § 45.103 of the Texas Education Code authorizes the District to issue time warrants. The warrants must mature in not more than 5 years from their date of issuance and are payable out of any available funds of the District. No election is required to issue time warrants. Time warrants may be issued to provide funds to construct, repair, or renovate school buildings, purchase school buildings and school equipment, or equip school properties with necessary heating, water, sanitation, lunch room, or electric facilities. The District may not have more than $500,000 in time warrants outstanding at any one time.

E. Contractual Obligations - The District is authorized to incur contractual obligations under chapter 271 of the Local Government Code to pay for school buses, computers, furniture and other moveable personal property. These contractual obligations are payable from maintenance taxes. The maturity of a contractual obligation may not exceed 5 years.

F. Lease Purchase Agreement - The District is authorized to form a Public Property Finance Corporation under Chapter 303 of the Local Government Code. This corporation has the authority to issue bonds to construct any necessary facilities for the District without an election. These bonds are secured by lease payments, payable from the District's maintenance tax and any other lawfully available funds, paid by the District to the Corporation.

G. Revenue Bonds - Under § 45.032 of the Texas Education Code, the District is authorized to issue revenue bonds to provide funds to acquire, construct, improve, or equip gymnasia, stadia, or other recreational facilities payable from and secured by liens on and pledges of all or any part of any of the revenues from any rentals, rates, charges, or other revenues from any or all of the facilities.

H. Refunding Bonds - Chapter 1207, Texas Government Code, authorizes school districts to refund or refinance all or any part of the district's outstanding bonds and matured or unmatured but unpaid interest on those bonds payable from ad valorem taxes by issuing refunding bonds payable from ad valorem taxes.

V. Debt Finance Guidelines - The District will consider a range of debt structures which when combined allow for flexibility in responding to future needs, do not utilize all available debt capacity, continue to emphasize credit considerations, and match well with the useful life of the assets for which debt is incurred.

A. Debt is a financing tool which should be judiciously used within the District's legal financial and debt market capacities.

B. Debt Defined - The creation of debt occurs when a governing body incurs a financial obligation that cannot or will not be repaid from current year revenues.

   1. Cash Flow Financing - Cash flow financing refers to tax and revenue anticipation notes (TANS and RANS) that are issued in anticipation of the receipt of revenues, and the tax dollars are levied, appropriated, and expected to be received in the fiscal year in which the note is issued. TANS and RANS are payable from current year revenues and, therefore, do not constitute debt.

   2. Short-Term Debt - For purposes of this policy, short-term debt refers to debt with a repayment term of less than five (5) years.

   3. Long-Term Debt - For purposes of this policy, long-term debt refers to debt with a repayment term greater than the maximum term of short-term debt, up to the maximum term allowable by law.

C. Conditions for Which Long-Term Debt May Be Issued - When an asset's useful life is appropriate for long-term financing and the estimated future revenues are sufficient to insure repayment of debt obligations, long-term debt will be considered.

   1. Bonds - Capital requirements for the construction, acquisition, and equipping of school buildings, and the purchase of necessary sites for school buildings will be identified and formalized in a capital improvement program (CIP) subject to voter approval. The capital planning process may incorporate updated demographic data from a third party consultant, facility planning data from administration and architectural firms, and debt financing data from the District's Financial Advisor and Assistant Superintendent for Business and Finance.

   2. Debt Refunding - The refinancing and/or restructuring of debt can be valuable debt management tools to provide the District with debt service savings or debt payment relief. Debt is often restructured through the issuance of refunding bonds. Current refunding occurs when the refunding bonds are settled within 90 days of an optional prepayment date. Advance refunding occurs when the refunding is settled more than 90 days in advance of an optional prepayment date. Federal restrictions allow an issue to be advance refunded only once on a tax exempt basis. The District will actively review, analyze, and pursue opportunities to refund outstanding debt.

   3. Variable Rate Debt - Variable rate debt can be an important tool in managing a debt program. When issued prudently, variable rate debt may help lower the cost of borrowing and provide a hedge against interest rate risk. Interest rates on variable rate debt instruments are at the short end of the yield curve because they are periodically adjusted (e.g. daily, weekly, or monthly) based on current market conditions. Variable rate debt gives investors the right to "put" securities back to the issuer at their discretion at specified future intervals. When issuing variable rate debt (rather than fixed rate debt), the District will need additional parties involved

including a Remarketing Agent, Liquidity Provider and Tender Agent. The Remarketing Agent determines the interest rate for the period, notifies the bondholders (through the Tender Agent) and remarkets any bonds tendered to either different bond buyers or the Liquidity Provider. The Liquidity Provider is usually a national or multi-national bank that provides the District with liquidity through a Standby Bond Purchase Agreement. Should there be a failed remarketing, the Bonds would be placed with Liquidity Provider until the bonds could be effectively remarketed. The Tender Agent would accept the tender bonds from the holders and notify the District, remarketing agent, liquidity provider and the bond holders of required mandatory or optional tender notices or rate changes.

As a general rule, some rating agencies recommend that variable rate debt not exceed 10-20 percent of total bonds outstanding, although other factors may affect their evaluation of the amount they regard as acceptable. The District may consider issuing variable rate bonds when variable short-term interest rates are consistently lower than long-term fixed rates. Total variable debt may not exceed 10% of the total outstanding debt, plus the amount of authorized bonds.

4. Unauthorized Structures - The District will not utilize swaps and other similar derivative products as a method of issuance.

D. Restrictions/Limitations of Debt Issuance:

1. Maintenance Tax Limitations - A school district is authorized to levy maintenance and operation taxes subject to approval of a proposition submitted to district voters under Section 45.003(d) of the Texas Education Code as amended. Subject to limited exceptions, the maximum tax rate that may be approved by voters for maintenance and operations is $1.50 per $100 of assessed valuation. For fiscal year 2008-09 and thereafter, the Commissioner is required to determine the state compression percentage for each fiscal year, which is based on the amount of State funds appropriated for distribution to a district for the current fiscal year. Furthermore, a school district cannot annually increase its tax rate in excess of the district's "rollback tax rate" without submitting such tax rate to a referendum election and a majority of the voters voting at such an election approving the adopted rate.

2. Debt Tax Limitations - The District will evaluate debt limitations in developing debt issuance plans. School districts are authorized to issue bonds and levy taxes for repayment subject to voter approval of a proposition under § 45.003(a) of the Texas Education Code. § 45.003(b)(1) provides for a tax levy unlimited as to rate or amount for the support of school district bonded indebtedness. § 45.0031 requires a district to demonstrate to the Texas Attorney General that it has the ability to pay debt service on the proposed bonds and all previously issued bonds from a tax at a rate not to exceed $0.50 per $100 of assessed valuation before bonds may be issued. A district may take into account State Allotments in demonstrating the ability to pay debt service at a rate of $0.50, but if Tier One allotments are used to pass the $0.50 test before a District can raise the Interest and Sinking (I&S) tax rate above the $0.50 level, it must apply the amount of Tier One funds as used to pass the test originally.

3. Maturity Levels - The weighted average life of the debt issuance should not exceed the useful life of the asset being financed, and in no case shall the final maturity of the issuance exceed the legal maximum of 40 years.

4. Repayment Provisions - The District will structure its debt in compliance with all federal, state, and local requirements as to repayment terms and seek to repay its debt in an expeditious manner within the District's overall financial objectives and in consideration of the useful life of the project and dedicated repayment revenue sources. The District will structure its debt with two primary goals: 1) to ensure the earliest possible maturity of the bonds, and 2) matching or improving upon the I&S tax rate assumptions and projections as discussed with the citizens of the District at the time of the bond election.

E. Debt Issuance Process:

Preferred Method of Sale - The District may use competitive sales, negotiated sales, or private placement as methods of sale for its debt issuance. When considering the method of sale, the District will take into consideration:

a. Financial and market conditions;
b. Transaction specific conditions; and
c. District related conditions.

Competitive sales are the preferred method under the following circumstances:

a. A general obligation pledge;
b. Simple structure and financial analysis;
c. Stable financial markets; and
d. Moderate par amount.

Negotiated Sales are the preferred method under the following circumstances:

a. Complex transactions that require extensive financial modeling, credit analysis, pre-marketing efforts, or that are interest rate sensitive; and
b. Volatile financial markets.

Private Placement is the preferred method under the following circumstances:

a. Smaller issue size; and
b. Overall cost savings to the District.

Reimbursement Resolution - As provided by law, the District may decide that it is in the District's best interest to pass a Reimbursement Resolution prior to the formal issuance of debt. The purpose of such a resolution is to announce the intent to reimburse itself for expenditures related to the capital programs for which debt may, or will, be issued. This would allow the General Fund, or whichever fund the original expenditures were made from, to be reimbursed by bond proceeds once the debt is issued. The District will intend to reimburse itself within 18 months from the later of the date the original expenditures or the date the project financed is placed into service.

1. External Financial Professionals:

   a. Financial Advisor - The District's Financial Advisor will work with District staff to:

      - Insure that the District's bonds are issued at the lowest possible interest cost and are structured in accordance with the District's financing guidelines;
      - Prepare the Notice of Sale, Preliminary Official Statement, and the Official Statement;
      - Obtaining the Permanent School Fund Guarantee through the Texas Education Agency or assist with other credit enhancement if needed;
      - Evaluate the bids submitted and recommend that they be accepted or rejected;
      - Review draft closing documents and monitor the closing process;
      - Prepare and submit the District's Annual Disclosure Report in accordance with SEC Rule 15c2-12; and
      - Assist in establishing repayment schedules that complement existing requirements and maintain a repayment pace acceptable to credit rating agencies.

   b. Bond Counsel - The District's Bond Counsel will:

      - Certify that the District has the legal authority to issue bonds;
      - Prepare required orders, resolutions, and tax certificates;
      - Work with the Attorney General to obtain approval of the bond issue;
      - Provide a legal opinion as to the enforceability and the federal income tax implications of the bonds; and
      - Coordinate the closing transactions.

   c. Paying Agent/Registrar - The District's Paying Agent/Registrar will:

      - Authenticate the bonds;
      - Send/receive transfers of money at closing;
      - Maintain a listing of bondholders and applicable addresses;
      - Receive principal and interest payments from the District and remit to bondholders; and
      - Represent bondholders in case of default.

   d. Rating Agencies - The District will consider obtaining a credit rating from at least one nationally recognized bond rating agency on its bond issues. There are currently three nationally recognized rating agencies: Moody's Investors Service, Inc., Standard & Poor's Rating Agency, and Fitch Ratings, Inc. Rating agencies assign a credit rating to bonds based on their assessment of the District's financial position and ability to make full and timely payments of principal and interest, and provide a ratings report to the market prior to the sale.

2. Timing of Sales - The District's Financial Advisor will work with the District staff (Assistant Superintendent for Business and Finance) to insure that the timing of bond sales coincide with having bond proceeds available for projects prior to the execution of constructions or purchase contracts.

3. Bond Rating Goals - The District will strive to maintain excellent bond ratings through:

   a. Strong financial management practices;

   b. Timely disclosure of annual financial information, including Annual Financial Report prepared by management and attested to by the external auditors; and

   c. Maintaining good relationships with bond rating agencies, including site visits or meetings in person when required.

4. Disclosure Requirements - The Securities and Exchange Commission (SEC) regulates both primary disclosure (the initial marketing of bonds and continuing disclosure (the ongoing information to the market about the status of the issue and issuer). The Securities and Exchange Commission Rule 15c2-12, as amended, requires the District to provide updated annual financial information no later than February 28th to the MSRB via the Electronic Municipal Market ("EMMA") system at www.emma.msrb.org. Timely and accurate information can improve the marketability of the District's bonds.

   The District will work with our Financial Advisor to prepare and file the annual report with the MSRB in order to fully comply with regulations.

VI. Management of Bond Proceeds - When bonds are issued, the proceeds are deposited in various accounts, which may include a construction fund, debt service fund, and an escrow fund in a refunding. Monies allocated to these funds are invested until needed. The investment strategy for each fund will depend, in part, on federal and state statutes and regulations governing the types of instruments permitted to be used, the yield permitted for the fund, and the anticipated drawdown of bond proceeds. Investment of bond proceeds shall be in accordance with the Public Funds Investment Act (PFIA) (Texas Government Code 2256), the Public Funds Collateral Act (Texas Government Code 2257), federal and state laws, and Policy CDA Local according to the cash flow schedule for capital projects. The District's Financial Advisor may not bid on investment products. Interest income generated from bond proceeds will be transferred from the Capital Project Fund(s) to the Debt Service Fund for the purpose of paying principal and interest costs on current and future debt.

The District will incur within six months of the date on which proceeds are issued, a binding obligation to a third party to expend at least five percent of the sale proceeds of the Bonds on a Bond Project. The District reasonably expects that work on or acquisition of the Project will proceed with due diligence to completion and that the proceeds of the Bonds will be expended on the Project within reasonable dispatch. The District reasonably expects that 85 percent of the sale Proceeds of the Bonds will have been expended on the Project prior to the date that is three years after the Issue Date. Any Sale Proceeds not expended prior to the date that is three years after the Issue Date will be either invested at a yield not "materially higher" or make yield restriction payments not less often than every fifth anniversary date of the delivery of the Bonds and within 60 days following the final maturity of the Bonds.

VII. Management of Debt Service Fund - The District has created or continued a debt service fund (the "Debt Service Fund") and the proceeds from all taxes levied, assessed, and collected for and on account of bonds are to be deposited in such Fund. The District expects that taxes levied, assessed and collected for and on account of bonds will be sufficient each year to pay such debt service. The Bona Fide Portion of the Debt Service Fund will be used primarily to achieve a proper matching of revenues and principal and interest payments on bonds within each bond year. Amounts held in the Bona Fide Portion of the Debt Service Fund will be invested at an unrestricted yield because such amounts will be expended within13 months of the date such amounts are received. The remaining portion of the Debt Service Fund (the "Reserve Portion") will be included in the calculation of arbitrage rebate.

A. Interest Earnings - Interest earnings in the Construction Fund may be used for project costs, principal and interest costs and related fees. Earnings of the Debt Service Fund will be used to pay only principal, interest costs, and related fees on current and future debt.

B. Unreserved, Undesignated Fund Balance - The District will target a minimum debt service fund balance of 25% of the annual debt service requirements on all outstanding debt issuance.

VIII. Compliance

A. Compliance with Statutory Regulations - The District will comply with all statutory regulations in the issuance and structuring of debt obligations.

B. Federal Arbitrage and Rebate Compliance - The District will follow a policy of full compliance with all arbitrage rebate requirements of the Internal Revenue Code of 1986, as amended, and its adopted rules and regulations, and will perform (via contract consultant) arbitrage calculations for each debt issue subject to rebate on an annual basis. All necessary rebates liability will be filed and paid when due.

C. Continuing Disclosure - The District will comply with the continuing disclosure requirements ads found in SEC Rule 15c2-12, as amended, to annual disclose certain operating data as well as audited financial statements. Also in accordance with this Rule, the District will file Material Events Notices as required.

IX. Reporting to Committee/Board - The Superintendent, Assistant Superintendent for Business and Finance, and the District's Financial Advisor will provide summary debt management reports to the Board at a minimum annually or with every bond sale. The Debt Management Policy will be reviewed on an annual basis and updated as needed.