Model Debt Management Policy + Guidance

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Though most Vermont municipalities take a very conservative approach to debt, a formal debt management policy can be an important financial management tool for town government. When debt is issued, it obligates the municipality to make regular payments for a number of years into the future. As a result, debt service can impact a town's financial condition over the long term and can limit flexibility to respond to changing needs and priorities.

Vermont law provides a very high ceiling for the limit of municipal debt. According to 24 V.S.A. § 1762, a municipality may not incur an indebtedness for public improvements which, with its previously contracted indebtedness, in the aggregate exceeds ten times the amount of the last grand list. Other statutes on municipal borrowing authority are found in V.S.A. 24, Chapter 53.

A municipal debt management policy will provide written guidelines affecting the amount, issuance, process, and type of debt. A debt management policy establishes criteria for issuing debt obligations so as not to exceed acceptable levels of indebtedness. Debt management policies transmit a message to the public and investors that the municipality is committed to sound financial management. These policies can also provide consistency and continuity in the debt issuance process.

The following should be considered in the development of a debt management policy:

Conditions for Debt Issuance. A debt management policy should specify the conditions or purposes for which the issuance of debt will be proposed by the selectboard, including the purposes and uses of each type of debt, the types of debt that will be utilized (short-term borrowing, capital lease agreements, general obligation bonds, etc.), life of assets acquired with each type of debt, and conditions for refunding debt.

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Restrictions on Debt Issuance. Debt management policies should also indicate any restrictions or limitations that are placed on the use of debt, including any prohibited uses, any limitations on the size of each issuance, limitations on the length of maturity for different types of projects, and any statutory limits on the amount of debt that can be issued.

Debt and Debt Service Limits. A limit on the amount of outstanding debt that is allowed should be included in the policy. This limit can be expressed in terms of a percentage of assessed value or as an amount per capita. A limit on the amount of annual debt service (principal and interest) should also be specified. This limit can be expressed as a percentage of revenues or expenditures, including coverage requirements for revenue debt, or as an amount per capita.

Characteristics of Debt Structure. Debt management policies should address the structure of debt issuance, including repayment provisions (level principal payments or level debt service payments), maturity guidelines, the use of debt service funds, and the investment of any bond proceeds (including a discussion of arbitrage regulations).

Debt Issuance Process. Most municipalities in the state utilize the Vermont Municipal Bond Bank to issue general obligation debt, so their procedures detail the debt issuance process. Under other circumstances, the debt management policy would include discussion of the sale process, the use of professionals to assist in the issuance process, bond rating goals, disclosure requirements, and rating agency relations.

For more information on debt management policies, please refer to ***Financial Policies: Design and Implementation***, published by the Government Finance Officers Association. A copy of this document can be purchased at www.gfoa.org(opens in a new tab).

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