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How Debt Managers View Debt Policies

by Bill Simonsen, Mark D. Robbins, and Bill Kittredge

The Government Finance Officers Association and others have espoused the use of debt policies as a useful tool for state and local governments to provide guidelines in debt issuance and management. However, precisely how much importance local government finance officers place on debt policy factors has been unclear. Therefore, in a recent study (Simonsen, Robbins, and Kittredge 2001) we set out to determine whether including a particular item, such as disclosure to bond-rating agencies and other interested parties, in a debt policy influences its perceived importance. Our research question was "Does the inclusion of an item in a debt policy make it more likely that managers in that government will view it as important?"

In order to answer this question, we surveyed local government debt issuers. The governments surveyed were drawn as a systematic random sample of general-purpose local governments (cities or counties) that sold new money municipal debt from July 1994 to August 1995, as listed in *Bond Buyer* (the national trade paper for the municipal bond industry). Governments refunding existing debt were not included in the sample.

The study addressed the question "Does the inclusion of an item in a debt policy make it more likely that managers in that government will view it as important?"

The debt policy section asked respondents to rank 20 factors in terms of how important they would consider them to be when selling debt (see table). They were to rank the factors on a scale of 1 to 5, with 5 indicating "extremely important." Respondents were also asked to indicate which factors are included in their own debt policies. We then compared the means of these scores, the overall means, with the means in those cases in which the policy element was already a part of a jurisdiction's debt policy.

Comparison of Means	Importance to Debt Managers	
Debt Policy Element	**Overall Mean**	**Mean if in the Debt Policy**
Responsibility to taxpayers (ratepayers) to get the lowest possible interest rate	4.73	4.75
Non-use of long-term debt to finance current operations	4.73	4.97
Debt service on bonds to not exceed the expected life of the project being financed	4.60	4.84
Avoidance of the appearances of an unfair process	4.59	5.00
Investment of capital funds or money in debt-service accounts in low-risk instruments	4.38	4.68
Disclosure to bond-rating agencies and other interested parties	4.29	4.64
Amount of the operating budget appropriate to use for servicing debt	4.17	4.54
Appropriate mix of current revenue and debt to finance projects	4.13	4.48
Routine use of competitive sales	4.03	4.42
Amount of debt to be retired over a specified period of time, e.g., 5 or 10 years	4.01	4.36
Acceptable debt-to-property value ratio	3.86	4.68
Appropriateness of increasing, level, or declining debt service	3.82	4.40
Inclusion of citizens in the decision-making process through public meetings, a vote, or other means	3.82	4.58
Linking the payment of the debt service to those groups benefiting from the project	3.56	4.70
Appropriate use of variable rate debt	3.21	4.58
Appropriate debt-to-property value ratio including all the governments that overlap your government	3.18	4.33
Explicit consideration of how the payment of the debt service will affect low-income groups	3.07	N/A
Routine use of negotiated sales	2.83	2.82
Use of request for proposal each time to hire financial advisors, underwriters, or others to help with debt sales	2.78	3.85
Inclusion of women and/or minority business enterprises in the bond sale process	2.58	4.00

Note: Mean is the mean score for this policy element. Elements were ranked on a scale of 1 to 5, with 5 indicating that they were considered "extremely important."

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The table presents our findings. It should be noted that among the policy elements that received the lowest scores were several related to assuring fairness and propriety (e.g., using a request for proposal [RFPs] and including women- and minority-owned businesses). Certain important "good government" principles become more important in the debt sale decision process when included in a debt policy. Our research highlights this effect most dramatically in the two cases mentioned: (1) the use of an RFP had an overall mean of 2.78 that rose to 3.85 when that factor was included in a debt policy; and (2) the inclusion of women and/or minority business enterprises in the bond sale process had an overall mean score of 2.58 but jumped to 4.00 when included in a debt policy. In sum, the presence of a debt factor in a debt policy made a significant difference in its perceived importance: 14 out of 19 factors showed a significant increase in importance if the policy element was present, even when controlling for other important factors (e.g., type of government, manager training, experience).

Certain important "good government" principles become more important in the debt sale decision process when included in a debt policy.

In times of decreasing public trust in government, the appearance or perception of government actions is at least as important as operating within legal standards. We suggest that a debt policy should be more than simply an aid to achieve legal compliance or to obtain the lowest interest rates possible. It should also address concerns about propriety, fairness, and accountability. In the survey, however, these tended to be among the least important factors to public managers.

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Our research showed that in the majority of cases the fact that items were included in a debt policy led public managers to think that these items were more important. This evidence suggests that it would be constructive to include elements related to ethics and accountability in a debt policy. Doing so would be consistent with assumptions implicit in the use of a debt policy and would offer some hope that use of such a policy could in fact improve both the practice and the perception of governance.

Selected Resources

Simonsen, Bill, Mark D. Robbins, and Bill Kittredge. 2001. "Do Debt Policies Make a Difference in Finance Officers' Perceptions of the Importance of Debt Management Factors?" *Public Budgeting and Finance* 21, no.1 (Spring): 87–102.

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