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SFA BILL ANALYSIS

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Senate Bill 1344 (as introduced 9-20-00)
Sponsor: Senator Joanne G. Emmons
Committee: Finance

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CONTENT

The bill would create the "Revised Municipal Finance Act" to regulate borrowing by and issuing of "obligations" by municipalities and prescribe the powers and duties of the Department of Treasury to protect the credit of the State and its municipalities.

Under the bill, a municipality would be a county, township, city, village, school district, community college district, metropolitan district, port district, drainage district, district library, or another governmental authority or agency that had the power to issue an obligation. "Obligations" would mean evidences of indebtedness such as bonds, refunding bonds, notes, contracts or assessments for the payment of bonds or obligations, and other similar instruments issued or incurred by a municipality, that were general obligations of the municipality, or that, on their face, pledged the limited tax full faith and credit of the municipality, or were payable primarily or secondarily from taxes, or special assessment, or both.

Department Powers

The Department of Treasury would be authorized to do the following:

-- Aid, advise, and consult with any municipality with respect to fiscal questions arising from and relating to its proposed or outstanding indebtedness.
-- Adopt rules as necessary to carry out the purposes of the proposed Act.
-- Examine the books and records of any municipality for the purpose of ascertaining if it was complying with the requirements of the Department, the statutes of the State, and its charter, ordinances, and resolutions, in relation to its obligations. The Department would have full power to examine witnesses on oath, and compel the attendance of witnesses, the giving of testimony, and the production of books, papers, and records. Any person duly subpoenaed who neglected to attend or testify would be guilty of a misdemeanor.
-- Enforce compliance with any provision of the Act or any law, charter, ordinance, or resolution with respect to obligations subject to its jurisdiction including the levy and collection of taxes for the payment of obligations.
-- Render financial advisory, paying agent, registration, and transfer services and materials, including assistance in the preparation and issuance of a municipality's obligations; prepare explanatory manuals; conduct training seminars; and, upon request of a municipality, assist the municipality in issuing its obligations. The Department could impose a fee upon municipalities requesting its services or materials, which would be limited to the cost incurred by the Department in providing the service.

If any municipality were aggrieved by any determination of the Department, it could notify the Department and appeal the determination as a contested case pursuant to the Administrative Procedures Act.

General Provisions

The bill would prohibit a municipality from borrowing money or issuing obligations except in accordance with the proposed Act.

Obligations authorized by law to be issued by a municipality could, notwithstanding the provisions of a charter, bear rates of interest at a maximum rate established by the governing body of the municipality, but the rate could not exceed 18% per year. Further, obligations could not be sold at a discount exceeding 10% of the principal amount of the obligations.

Obligations could be sold at a public competitive sale or a public negotiated sale as determined in the authorizing resolution. Obligations to be sold at a public competitive sale could be sold only after notice by publication, at least seven days before the sale, in a publication printed in the English language and circulated in the State. Bids at a public competitive sale would have to be selected on the basis of the lowest total interest cost. Within seven days of the issuance of an obligation, a municipality would have to notify the Department of the details of the issue in a manner determined by the Department.

The governing body of a municipality could provide for an obligation to be registerable, authenticated, transferred in ownership, or exchanged (if mutilated) as provided in the bill.

Municipality Powers

The bill would allow a municipality, in determining to issue obligations, to do the following:

-- Authorize and enter into transactions to provide security for the timely payment of obligations, including insurance contracts and lines of credit.
-- Authorize payment of the cost of issuance of an obligation from the obligation's proceeds or other funds.
-- Authorize principal and interest to be payable from taxes or other revenues; obligation proceeds and earnings on the proceeds; and proceeds of any other security.
-- Authorize an officer of the municipality to perform various specified duties in relation to selling, buying, and delivering obligations.

A municipality that issued obligations in anticipation of special assessments could, notwithstanding any charter or ordinance provisions to the contrary, in order to pay principal and interest on the obligations, charge a rate of interest on the unpaid balance of the special assessments in excess of the charter or ordinance limit but not in excess of 1% above the average rate of interest borne by the obligations.

A municipality could enter into an interest rate exchange, swap, hedge, or similar agreement, to manage its debt service. The bill provides that an agreement would not be a debt of the municipality for purposes of statutory or charter limitations; and would be payable as a limited tax general obligation from the general funds of the municipality.

Local Drains

The bill provides that any county, township, city, or village, by resolution of its governing body and without a vote of its electors, could issue its full faith and credit obligations for the purpose of funding any or all of a county or intercounty drain special assessment made under the Drain Code. The bill specifies the requirements that the obligations would have to meet.

Water and Sewer/Federal Purchase

The bill provides that when an obligation issued for the purpose of defraying the cost of purchasing, acquiring, constructing, or improving any water supply or sewage disposal system was purchased at competitive sale or negotiated sale by the Federal government, and applicable rules of the Federal government so required, "serial obligations" comprising the obligations could be delivered to the Federal government in installments. Installment deliveries would have to be made during the construction or improvement of the system in an amount calculated to be sufficient to defray expenses to be incurred prior to the next scheduled installment delivery. Payment in an amount equal to the aggregate par amount of obligations delivered in each installment would have to be made at the time of delivery of each installment. If the Federal government required, interest coupons representing interest due on the obligations from the date of delivery to the first interest payment date could be adjusted. "Serial obligations" would be any series of obligations maturing in two or more installments, or in one installment within three years from the date of issuance.

Obligations for Insurance

The bill would allow a municipality by resolution or intergovernmental contract, without a vote of the electors, to issue its full faith and credit limited tax obligations, which could not be considered debt of the municipality for statutory, charter, or constitutional debt limitations, but could not require or authorize the levy of taxes in excess of applicable statutory, charter, and constitutional debt limitations, for the following purposes:

-- Paying premiums and other charges for coverages provided by an insurance pool established pursuant to Public Act 35 of 1951, or evidencing fixed payment obligations or obligations to make payments under specified contingencies pursuant to an intergovernmental self-insurance pool contract approved by the State Treasurer under that Act. (Public Act 35 of 1951 allows two or more municipal corporations (any local government or local agency with the power to enter into contracts) to form a group self-insurance pool to provide mutual risk for various types of insurance as provided under the Act.)
-- Establishing funds, reserves, or accounts in amounts determined by the municipality to defray losses for which insurance coverage could be provided by an insurer pursuant to the Insurance Code, but for which the municipality determined to self-insure.

An obligation issued under these provisions could not exceed 30 years. The bill specifies further requirements that the obligation would have to meet.

Tax Anticipation/Debt Retirement

The bill would allow a municipality, by resolution and without a vote of the electors, to borrow money and issue its obligations in anticipation of the collection of the taxes, revenue sharing payments under the Glenn Steil State Revenue Sharing Act, and other revenues prescribed in Part IV (Tax Anticipation Obligations) of the proposed Act.

If the money borrowed by the municipality were for operating expenses, it could be used only for the purpose of paying the necessary operating expenses of the municipality, which could not reasonably have been foreseen and adequately provided for in the tax levy for the then current fiscal year; for the payment of an expense in the current fiscal year that could not be funded because of a delay in or failure of receipt of budgeted revenue; or for the payment of budgeted expenses in the current fiscal year that preceded budgeted revenues. The amount to be borrowed for these purposes could not exceed 50% of the operating tax levy for the current fiscal year, or if the operating tax levy for the next succeeding fiscal year were determined, 50% of the levy for that fiscal year. The bill also would require the authorizing resolution to provide for a portion of the taxes to be set aside in a special fund for the payment of principal and interest. The taxes set aside could not be used for any other purpose. If money were borrowed for capital improvements, a portion of the taxes would have to be set aside in a special fund for the payment of principal and interest on the tax anticipation obligations.

If borrowing were made in anticipation of the collection of taxes for a current fiscal year, the proceeds of the borrowing could be used only for the payment of operating expenses, debt service charges, or capital improvements. The amount of money borrowed for the payment of operating expenses or debt service charges would be limited as provided in the bill. Money borrowed for the payment of a capital improvement could be used only for the payment of the improvements provided for in the tax levy of the current fiscal year, and could not exceed the anticipated collection. Borrowing in anticipation of the receipt of revenue sharing payments could be used only for the payment of operating expenses.

The bill provides that if a municipality had obligations outstanding, or with the approval of its electors had authorized the issuance of obligations to be paid from collections of its next tax levy, it would have to include in the amount of taxes levied each year the following:

-- An amount such that the estimated collections would be sufficient to pay promptly, when due, certain interest and principal on the obligations, before the time of the following year's tax collection.
-- An amount, if there were outstanding term refunding obligations, sufficient to provide required sums to be deposited into the sinking fund for that purpose before the time of the following year's tax collection.
-- Certain amounts, which if deposited annually into a sinking fund would, with the existing sinking fund pertaining to the obligations and the increment of the obligations, be sufficient to pay the obligations at maturity.

The bill states that these provisions would not limit the amount required to be levied in a year for the purposes prescribed by the terms of an ordinance or resolution authorizing the issuance of the obligations. If the obligations were not approved by the electors of the municipality, the municipality would have to levy and collect ad valorem taxes as required under the bill for the payment of the obligations as a first budget obligation; however, the ad valorem taxes would be subject to applicable charter, statutory, or constitutional limitations.

If an annual tax levy for the payment of principal and interest resulted in surplus money, the annual levy could be reduced. Further, money remaining in a debt retirement fund from the levy of a tax after the retirement would have to be used first to pay other funded indebtedness of the municipality, next to pay any other debt of the municipality, and finally be dedicated to the municipality's general fund.

If taxes, special assessments, or both, had been levied for or pledged to the payment of obligations, all money on hand or thereafter received from these taxes and/or special assessments would have to be applied as prescribed by the authorizing resolution, and as might be approved by the Department.

Debt retirement funds would have to be kept separate from other money of a municipality and be used only to retire its funded indebtedness. When any municipality completed the retirement of outstanding obligations, or accumulated sufficient funds in the debt retirement fund for the retirement of the obligations, the governing body of the municipality would have to certify that the obligations were retired, or that the debt retirement fund was sufficient to retire the obligations.

Any municipality issuing term refunding obligations under the proposed Act would have to provide a sinking fund or funds for the retirement of those obligations, and deposit in each such sinking fund each year amounts sufficient to pay the principal of the obligations at or before maturity. All sinking fund money for the retirement of refunding obligations would have to be kept separate from the other sinking fund money and from all other money of the municipality and be used for no purpose except the payment or purchase of the refunding obligations.

Obligation Requirements

Except as otherwise provided in law or in the proposed Act, obligations issued by a municipality could not be issued for longer than the estimated period of usefulness of the property or improvement for which they were issued. In addition, obligations could not be issued for a longer time than the following:

-- For obligations issued in anticipation of special assessments, two years from the time fixed by law for the payment of the last installment of the assessments from which the obligations were payable.
-- For emergency obligations for relief from fire, flood, or other calamity, five years.
-- For obligations for payment of judgments against the municipality, except judgments in condemnation proceedings, and obligations for the purchase of personal property, other than material for permanent construction, machinery for public utilities, or original furnishings and equipment of new buildings, 10 years.
-- For obligations for sewage disposal, water, or transportation systems, or for the construction, opening, widening, or improvement of bridges, 40 years.
-- For obligations for the construction, opening, widening, or improvement of highways, streets, roads, or alleys, 30 years.

The bill specifies various maturity dates for serial obligations and term obligations. (A term obligation would be any series of obligations that matured in one installment after three years from the date of issuance.) The obligations of any series could be made redeemable as provided by ordinance or resolution of the governing body. A premium could not be paid on an obligation that exceeded 3% of its par value.

Interest that accrued on an obligation issued during the first three years after the date of the obligation could be paid from the proceeds of its sale. In addition, a reserve fund, in an amount up to 15% of the principal amount of the obligation issued, could be established from the proceeds of the sale of the obligation and be held solely for the payment of principal of, and interest on, the obligation.

The total amount of special assessment obligations of any township, city, or village pledging its limited tax full faith and credit could at no time by reason of future issues, other than issues of refunding obligations, exceed 15% of the taxable value of the taxable property in the municipality. Further, those obligations could not be issued in any calendar year in excess of 5% of the taxable value unless authorized by majority vote of the electors, or by a larger vote as provided by statute or charter.

Refunding

A municipality could by resolution and without a vote of the electors refund all or any part of its funded indebtedness by issuing refunding bonds. The bill specifies the circumstances under which refunding bonds could be issued. Refunding obligations could be secured by and payable from any of the following:

-- Taxes or special assessments pledged for payment of the obligations being refunded.
-- The proceeds of the refunding obligations.
-- The reserve, if any, established for the payment of the principal of, or interest and redemption premiums on, the refunding obligations or the obligations to be refunded.
-- The proceeds of any insurance, letter of credit, or line of credit acquired as security for the refunding obligations.
-- The proceeds of any obligations issued to refund the refunding obligations.
-- Investment earnings or profits on any of the sources described above.

Any outstanding funded indebtedness of a municipality that had been assumed in part by another municipality could be refunded by the municipalities as to their respective liabilities.

The bill states that it could not be construed to prohibit a municipality from refunding any of its outstanding funded indebtedness even though some other municipality could have become obligated to contribute to the payment of that indebtedness.

The refunding obligations and the tax levies used to repay those obligations could not be deemed to be within any statutory or charter limitation of tax rate, but would be authorized in addition to any statutory or charter limitation of tax rate or funded indebtedness.

Refunding obligations issued to refund drainage obligations issued under the Drain Code would be obligations of the same character as the obligations refunded, and would have to be construed as a continuation of the former obligations. Also, refunding obligations issued to refund former obligations secured by a pledge of unlimited taxes would have to be secured by an unlimited tax pledge. All other refunding obligations, unless otherwise provided, would be the general obligation of the issuing municipality and its full faith and credit would be pledged to payment of these refunding obligations.

Legislative Analyst: G. Towne

FISCAL IMPACT

State Impact: Under Senate Bill 1344, State revenues would be reduced because of the elimination of filing requirements and filing fees. Under current law, the Department of Treasury receives approximately $250,000 per year in fees from local units to review and approve bond sales. The bill also would reduce the Department of Treasury's oversight obligations regarding the issuance of local units' debt obligations.

Local Impact: Since local units would no longer be required to seek prior approval from the State for sales of bonds and other debt obligations, filing fees would decline by approximately $250,000 under the bill. Other provisions of the bill would allow local units to issue debt more easily or would increase the maximum amount of outstanding debt a local unit may hold. If local units took advantage of these provisions of the bill, then debt service payments by local units would increase under the bill.

The extent to which local units would increase debt issuance under the bill is unknown. One provision of the bill would increase the maximum allowable outstanding debt a local unit may hold for special assessments from 12% of taxable value to 15% of taxable value, as well as increasing the amount of debt that may be issued without a vote of the electorate from 3% to 5% of taxable value. In 1999, the taxable value of property in the State totaled $233.8 billion. If local units comprising 10% of the taxable value of the State were to issue additional debt of 3% of taxable value under the bill, at a 6% rate amortized over 30 years, then debt service payments under the bill would increase by approximately $51.0 million.

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