Legislative Analysis

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REFUNDING OBLIGATIONS

House Bill 5550 as enrolled
Public Act 321 of 2010
Sponsor: Rep. Jeff Mayes
House Committee: Banking and Financial Services
Senate Committee: Finance

Complete to 1-24-11

A SUMMARY OF HOUSE BILL 5550 AS ENROLLED

House Bill 5550 amended the Revised Municipal Finance Act (MCL 141.2611) to allow a municipality to refund all or any part of its outstanding securities by issuing a refunding security that would be exempt from the act's current requirement that the net present value of the principal and interest to be paid on the refunding security be less than the net present value of the principal and interest to be paid on the security being refunded. (The bill is understood to essentially allow local units of government to restructure existing debt by extending debt further into the future and lowering current debt payments.)

Under the bill, the refunding must be issued before December 31, 2012, and would only apply to securities that were not secured by the unlimited full faith and credit pledge of the municipality. The refunding must be approved by the Michigan Department of Treasury. A municipality is required to hold a public hearing on the refunding before seeking approval from the state. The bill says the department "shall not unreasonably withhold approval." The department would have to make its decision within 90 days or the municipality's request would be deemed approved.

Prior to the passage of this bill, the Revised Municipal Finance Act allowed an exception from the "net present value" requirement for refunding securities to be granted by the Department of Treasury on a case-by-case basis, with criteria for the exceptions spelled out in the act. For example, such refunding is allowed to avoid a potential default on an outstanding security. These provisions were retained. The provisions of the bill are in addition to those pre-existing exceptions.

BACKGROUND INFORMATION:

According to testimony, the proposed legislation provides a short-term solution to a problem municipalities are facing due to falling property tax revenues: incremental increases in revenues that were anticipated to support debt related to tax increment financing arrangements are not materializing. This potentially leaves local units without sufficient revenue to meet their obligations unless they use general fund dollars. Currently, refunding debt is typically permitted only if there is a present value interest savings. House Bill 5550 would instead essentially allow local units of government to restructure existing debt by extending debt further into the future and lowering current debt payments.

The Department of Treasury noted in its testimony that it could already allow negative net present value funding on a case-by-case basis, based on criteria established in statute, and expressed concern that the bills removed a level of review of local government financing that should be maintained. Earlier versions of the bill did not require Treasury approval; however, as enacted, the bill requires Treasury approval of the refunding securities described in the bill.

FISCAL IMPACT:

The fiscal impact of House Bill 5550 on state and local government is indeterminate. Its provisions expand the instances in which qualified refunding obligations may be used. Refunding obligations are issued to restructure or refinance the costs of an earlier debt obligation. The new obligations are often associated with lower interest and/or payment costs to the municipality or authority. Under this bill, municipalities will be able to lower debt payments and avoid using their general funds to meet current obligations. However, municipalities will face higher costs long-term by extending their debt further into the future by issuing refunding obligations.

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