2019
PUBLIC FINANCE HANDBOOK FOR TEXAS COUNTIES

TEXAS ASSOCIATION OF COUNTIES

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PREFACE TO THE 2019 EDITION

Our law firm is proud to present this 2019 edition of the Texas Association of Counties Public Finance Handbook for Texas Counties. The handbook is the creation of our partner Tom Pollan who retired from practice in 2018. Since founding the firm's public finance practice in 1988, Tom developed a well-deserved reputation as a leader in the field of public finance for Texas counties, and this version of the handbook retains virtually all of the information included in earlier editions that he had written.

Following the publication of the first edition in 2006, we have provided updates to the handbook every two years to address changes brought about through legislation and by new case law. Likewise, this edition of the handbook covers changes to the public finance statutes made by the Texas Legislature, as well as changes to federal securities law and federal tax law that affect the use of bonds by counties. Some of the most significant changes that are discussed in this handbook include:

1. Extension of the public notice period for the issuance of certificates of obligation from 30 days to 45 days (*See,* Article II, Section B.1, *Certificates of Obligation*);
2. Elimination of tax-exempt advanced refunding bonds (*See*, Article II., Section B.5, *Refunding Bonds*);
3. Additions to the information required in election orders and proposition language (*See,* Article IV, Section C.2, *Contents of the Election Order*); and
4. Addition of new continuing disclosure requirements under federal law (*See,* Article V, Section C, *Continuing Disclosure*).

References to case law, the constitution, regulations, and statutes in this edition of the handbook are current through September 1, 2019.

This work draws on not only the efforts of the firm's public finance group, but also on the insights offered by attorneys with the firm that focus on a range of issues directly relevant to the operations of county government such as development and procurement, elections, real estate, securities, and tax. We hope that this version of the handbook is useful for you and that it meets the same standards that Tom established in earlier editions. If you have any questions about the information in this handbook, please don't hesitate to get in touch.

I. Introduction and Overview

This handbook is designed to explain the bond issuance process, especially for counties that do not issue bonds on a frequent basis. A county that is not familiar with the issuance of debt obligations may anticipate the process to be complex, but it is in fact one that can be readily explained and understood. This handbook is intended to allow you to get a quick grasp of the fundamentals of county bonds and to identify the steps in the issuance bonds that will be most important to administrative staff and to the commissioners court.

A Texas county can finance projects in several ways. The most common are the issuance of General Obligation Bonds, Certificates of Obligation, Tax Notes, and Contractual Obligations. Generically, all of these methods can be called "bonds." Other financing methods used by counties are lease purchase obligations, public improvement district bonds, time warrants, and venue project bonds.

A county issues bonds to finance something over a period of time. As a political subdivision of the State of Texas (the "State"), a county cannot simply go to a bank and take out a loan, unless the loan is to be repaid within the current fiscal year. To borrow money beyond the current fiscal year, the county must issue a debt obligation—a security known as a bond which will be sold for cash in return for the county's promise to repay the debt obligation with interest, generally at a favorable tax-exempt interest rate.

In order to sell bonds a county must generally retain consultants to assist in the process. A financial advisor will structure the transaction and arrange the sale of the bonds to an underwriter or a bank. Bond counsel will prepare the bond order and other documents, shepherd the county's bonds through the attorney general's review process, provide an opinion as to the bond's validity, and if applicable, an opinion that the bond is a tax-exempt obligation for federal income tax purposes. Bond counsel and the county's financial advisor will also guide the county through the various tax and securities issues that are part of the bond issuance process. They also assist the commissioners court and other county staff in obtaining ratings, insurance, and securing necessary banking arrangements to complete the transaction.

This handbook will assist you in understanding the process. It begins with a description of the different purposes for which a county may issue debt and the forms that debt may take. Next is a high-level outline of the process for issuing debt, the parties involved in issuing debt, and the different documents that go into sale of debt. Following the outline of the transaction process, the rest of this guide looks at three significant aspects of county debt: the use of elections to approve debt, securities law as it relates to county obligations, and the federal tax law of tax-exempt obligations.

The definitions of terms appearing in this handbook in bold can be found in Tab 1. Also included in subsequent tabs to this handbook are the leading attorney general opinion on the issuance of debt by a local government, key constitutional provisions relating to county debt, Securities and Exchange Commission Rule 15c2-12, and suggestions for further reading.

This guidebook does not address every question that can come up regarding the structuring of a debt transaction, and it is not intended as legal advice. We do expect, however, that it can be of some use in your county's decision making process.

II. <u>Authorized Purposes of Debt and the Types of Debt Obligations Available to Texas Counties</u>

Key Points

- *A county must have express constitutional or statutory authority to issue "**debt.**"*
- *"Debt" generally means any obligation that cannot be paid out of the current budget.*
- *This section of the handbook lists the authorized purposes for issuing debt and describes the different forms of debt available to counties.*

A. Authorized Purposes of County Debt.

For all local governmental entities in this State, the authority to issue "**debt"** must be expressly granted by the Texas Constitution or statute. (For a detailed treatment of this concept, see Texas Attorney General Opinion No. JC-0139, included as Tab 2.) For the purposes of state law as it applies to a county's ability to borrow money, a "debt" is any financial obligation incurred by a county that is not expected to be fully repaid from out of the current budget, or from funds immediately available to the county. Therefore, short-term borrowing that is paid back within the year is generally not considered the creation of a debt for constitutional purposes, whereas any loan obligation that extends beyond the county's fiscal year is a debt which requires statutory authorization. To keep matters simple, this handbook uses the same legal definition of the term "debt." As such, whenever the word "debt" appears in this handbook, it means "any monetary contractual obligation of a county that cannot reasonably be expected to be repaid out of current revenues for the year or from immediately available funds." As seen in this handbook, the term includes instruments such as general obligation bonds, certificates of obligation, and tax notes.

The legislature, using the authority granted by the Texas Constitution, has provided counties with a variety of mechanisms to issue debt to allow commissioners courts to address community needs. Each approach provides the county with a solution to target a particular situation. With this authority, the commissioners court and its financial advisor and bond counsel can select a particular type of debt that is tailored to take care of the county's needs in the best way.

The following table lists the specific purposes for which a county may issue debt and the relevant statutory authority.

Authorized Purposes for Issuing Bonds and Certificates of Obligation

Purpose	Source of Statutory Authority
Acquisition of real property for county purposes, including right-of-way	Local Government Code §§271.041 et seq **(Certificates of Obligation)**
Acquisition of public housing from federal government	Local Government Code §270.004(d)
Agricultural experiment farms and substations	Agriculture Code §43.007(b)
Air pollution control facilities	Health & Safety Code §§383.021 et seq
Airports	Transportation Code §22.052
Civic center and related facilities	Government Code §§1473.171 et seq; §§1477.301 et seq
Construction of any public work	Local Government Code §§271.041 et seq **(Certificates of Obligation)**
County office buildings	Government Code §1473.101(a)(1) Local Government Code §292.002
Courthouses and jails	Government Code §1301.001(a)(1)
Crime detection facilities	Government Code §§1473.052; 1473.053 Government Code §1473.231 (counties with populations of more than 900,000)
Firefighting equipment	Government Code §1477.151

Purpose	Source of Statutory Authority
Homes and farms for the needy and indigent	Government Code §1301.001(a)(3)
Homes and schools for dependent and delinquent children	Government Code §1301.001(a)(3) Human Resources Code §152.036 (Dallas Co.) Human Resources Code §152.1076 (Harris Co.)
Horticultural and agricultural exhibit halls	Government Code §§1473.171 et seq; 1473.021 et seq
Hospitals	Health & Safety Code §263.024 Local Government Code §280.003
Joint city-county criminal justice facilities	Local Government Code §361.003
Navigation aid improvements	Texas Constitution Art. III §52[1] Government Code §§1475.001 et seq
Parking facilities	Government Code §§1473.131 et seq
Parks	Local Government Code §331.004
Permanent library improvements	Local Government Code §323.052
Preparation of property tax surveys, maps and plats	Government Code §§1477.251 et seq
Professional services in connection with a public work	Local Government Code §§271.041 et seq **(Certificates of Obligation)**
Public health administration facilities (counties with populations of more than	Government Code §§ 1473.171 et seq

[1] Included at Tab 3

Purpose	Source of Statutory Authority
275,000)	
Public health units health and safety code	Health and Safety Code §§1477.251 et seq
Purchase of voting equipment	Election Code §123.031(b)
Reclamation and irrigation projects	Texas Constitution Art. III §52 Government Code 1473.131 et seq; §§1477.051 et seq
Renovation of county office buildings in county seat	Government Code §1473.052
Roads and bridges	Texas Constitution Art. III §52 Government Code §1301.001(a)(5); Chapter 1471; Chapter 1478; Transportation Code §251.083(b); Chapters 283, 284, and 364
Seawalls, breakers, and projects for sanitary purposes	Texas Constitution Art. XI §7[2] Local Government Code §§421.001 et seq
Solid waste disposal systems	Health & Safety Code §§363.051 et seq; §§383.021 et seq
Sports centers	Government Code §§1432.001 et seq; §§1473.171 et seq

B. Debt Instruments Available to Counties

There are various financial instruments available to a county, and different requirements exist for each type of instrument. Some require or may require an election while others do not. The length of time for the financing differs with the type of

[2] Included at Tab 3

instrument. The primary instruments counties use in ad valorem tax-backed financing are General Obligation Bonds, Certificates of Obligation, Contractual Obligations, Tax Notes, Time Warrants and Refunding Bonds. Lease Purchase Agreements and Revenue Bonds may also be used. The following is a discussion of each of these methods.

1. Certificates of Obligation

Certificates of obligation ("CO's") are a streamlined method of financing. They are authorized by the Certificate of Obligation Act of 1971, Subchapter C of Chapter 271 of the Texas Local Government Code. CO's are limited to certain statutory purposes, which cover most any financing that the county might need to do: (a) pay for construction of a public work; (b) pay for purchase of materials, supplies, equipment, machinery, buildings, lands, and rights-of-way for the issuer's authorized needs and purposes; and (c) pay for professional services such as engineers, architects, attorneys, and financial advisors.

CO's may be payable from ad valorem taxes, revenues or a combination thereof. Although a CO may be backed solely by a revenue pledge, traditionally if there is a revenue pledge involved, it is a limited pledge of surplus revenues to permit the CO's to be sold for cash, as explained below.

CO's may be amortized up to 40 years, just as General Obligation Bonds, which are defined and discussed in this Handbook below, but a shorter time frame is usually involved. The length of time that CO's will be outstanding should correspond to the useful life of the project being financed.

No Election Required Unless Valid Petition Presented

Unlike General Obligation Bonds that always require an election, CO's do not require an election unless at least 5% of the registered voters in the county submit a valid petition protesting the issuance. This should not be viewed as taking away the right to vote on a bond issue, but rather as a method to avoid the time and expense of an election unless the public determines that an election should be held before the CO's are issued. An election can only be held if a valid petition is received prior to the time the commissioners court votes to approve the issuance of the CO's. If a valid petition is received, the commissioners court cannot issue CO's until an election is held. The election is conducted in the same manner as a General Obligation Bond election.

To ensure that the public is informed of the possibility of the issuance of the certificates, the legislature requires that notice of intent to issue the CO's be published once a week for two consecutive weeks in a newspaper of general circulation within the county, with the first publication being not less than forty-five (45) days before the date tentatively set for passage of the order authorizing the issuance of the CO's. The notice and publication must be authorized by the commissioners court. The notice must specify:

(1) the time and place tentatively set for the passage of the order authorizing the issuance of the CO's;

(2) the maximum amount and purpose of the CO's to be authorized; and

(3) the source from which the CO’s will be paid, either from ad valorem taxes, revenues or a combination of taxes and revenues.

The date chosen for passage must be a regularly scheduled meeting date of the commissioners court, as the date of passage will also be the date for the sale of the CO’s.

CO’s Sold for Cash

CO’s can either be delivered to a vendor for the project or “sold for cash.” As a practical matter, COs are almost always sold for cash. When the COs are sold for cash, the county uses the proceeds of the sale of the COs, that is, the cash received, for the project and for the costs of issuing the COs.

A county may not sell COs for cash unless there is express statutory authority to do so. If the repayment of the COs is secured by only a tax pledge, COs may only be sold for cash for a specific set of purposes. The Certificate of Obligation Act, Local Government Code Chapter 271, Subchapter C, specifies the following situations where CO’s may be sold for cash without an additional pledge: (1) in the case of public calamity, it is necessary to act promptly to relieve the necessity of the residents or to preserve the property of the county; (2) it is necessary to preserve or protect the public health of the residents of the county; (3) in the case of unforeseen damage to public machinery, equipment, or other property; (4) it is for a contract for personal or professional services; (5) work is done by employees of the county and paid for as the work progresses; (6) it is for the purchase of any land, building, existing utility system, or right-of-way for authorized needs and purposes; (7) in the case in which the entire project is to be paid from bond funds or current funds or in which an advertisement for bids has previously been published in accordance with the Certificate of Obligation Act, but the current funds or bond funds are not adequate to permit the awarding of the contract and CO's are to be awarded to provide for the deficiency; or (8) in the case of a county contract that is not required to be bid under the County Purchasing Act.

Additionally, the Certificate of Obligation Act gives a county express authority to sell CO's for cash with only a tax pledge for (1) constructing or equipping a jail; (2) constructing, renovating, or otherwise improving a county-owned building; or (3) constructing a bridge that is part of or connected to a county road or an approach to such a bridge.

Although the listed authority to sell for cash with only a tax pledge covers many things a county might do, it does not address several items that a county most likely would need, including road construction and equipment acquisitions. To cover these situations, the Certificate of Obligation Act also authorizes CO's to be sold for cash if there is a revenue pledge included with the tax pledge. Generally, a limited pledge of revenues is made, such as an amount not to exceed $1,000 or some other specified nominal amount. There is no requirement or expectation that the pledged revenues will ever be used for debt service. Historically, revenues from county operations of various types such as landfill fees, library revenues, park revenues, or revenues for housing out-of-county prisoners, among others, have been used for this purpose. In order to pledge a revenue source, there must be statutory authority to pledge the revenues to support a bond issue. This would eliminate some revenue sources that at first glance might seem to provide a source for the pledge. Also, sales tax revenues are expressly excluded from being used as a pledge under a Tax Code provision.

Limitation on the Use of Certificates of Obligation After a

Failed Bond Election

In 2015, Section 271.047, Texas Local Government Code was amended to prohibit the use of CO's for the same purpose that had been presented to the voters in a bond election which failed within the three preceding years. The legislature provided that the three year prohibition on the use of CO's after a failed bond election does not apply to the following situations:

(1) a case of public calamity if it is necessary to act promptly to relieve the necessity of the residents or to preserve the property of the issuer;

(2) a case in which it is necessary to preserve or protect the public health of the residents of the issuer;

(3) a case of unforeseen damage to public machinery, equipment, or other property; and

(4) to comply with a state or federal law, rule, or regulation.

Competitive Bidding

Unless there is an exception, projects to be funded with proceeds from CO's must be competitively bid. The Certificate of Obligation Act contains its own competitive bid requirements which are similar to, but not exactly the same as, the County Purchasing Act. In 2011, the competitive bidding requirement for the Certificate of Obligation Act was amended to permit using the alternate construction delivery methods provided under Chapter 2269 of the Government Code, e.g. construction manager-agent method, design-build method, etc. Prior to this amendment, counties were prohibited from using these methods if a project was to be financed through the use of certificates of obligation. With the amendment, Section 271.054 now reads:

§ 271.054. Competitive Procurement Requirement

Before the governing body of an issuer may enter into a contract requiring an expenditure by or imposing an obligation or liability on the issuer, or on a subdivision of the issuer if the issuer is a county, of more than $50,000, the governing body must:

(1) submit the proposed contract to competitive procurement; or

(2) use an alternate method of project delivery authorized by Chapter 2267, Government Code.[3]

Purposes Combined

Unlike General Obligation Bonds which must have the items to be voted on listed separately, the purposes for CO's are combined. For instance, in a $7,000,000 bond issue, a county would need to have separate propositions on the ballot for the construction of a new jail, road improvements, courthouse improvements and a new communications system. The propositions would be in the following format:

Proposition 1. The issuance of $3,000,000 general obligation bonds to pay for the construction and equipping of a new

[3] The alternative delivery methods that were formerly found in Subchapter H of Chapter 271 of the Local Government Code were transferred to a new Chapter 2267 of the Government Code.

> county jail and the acquisition of a site
>
> Proposition 2. The issuance of $2,000,000 general obligation bonds to pay for the construction and improvement of county roads and bridges
>
> Proposition 3. The issuance of $1,500,000 general obligation bonds to pay for courthouse improvements
>
> Proposition 4. The issuance of $500,000 general obligation bonds to acquire a new communications system

With CO's, the county would provide in its notice of intent the following language:

> Authorize the issuance of the certificates of obligation in an aggregate principal amount not to exceed $7,000,000 for the purpose of paying contractual obligations to be incurred for (1) the construction and equipping of a new county jail and the acquisition of a site, (2) the construction and improvement of roads and bridges in the County; (3) construction of courthouse improvements; (4) acquisition of a new communications system; and (5) the payment of professional services and costs of issuance related thereto.

For example, if all the propositions for the General Obligation Bond issue were approved and bonds were issued, the county would be required to maintain the allocations. If the jail project cost $3,025,000 and the courthouse improvements only cost $1,475,000, the county could not transfer funds between the two items. With CO's, the county would not be precluded from making transfers from one item where there were surplus funds to an item where additional funds were needed.

2. Contractual Obligations

Contractual Obligations are a financing tool that is available to counties to finance personal property. They are authorized under Subchapter A of Chapter 271 of the Texas Local Government Code, the Public Property Financing Act, are payable from a pledge of revenues, funds or taxes, and may not be used to acquire real property. The definition of "personal property" is defined in Section 271.003(9), Texas Local Government Code:

> "Personal property" includes appliances, equipment, facilities, and furnishings, or an interest in personal property, whether movable or fixed, considered by the governing body of the governmental agency to be necessary, useful, or appropriate to one or more purposes of the governmental agency. The term includes all materials and labor incident to the installation of that personal property. The term does not include real property.

The Public Property Financing Act permits a county to enter into a contract to purchase personal property which may be in the form of a lease, a lease with an option or options to purchase, an installment purchase, or any other form considered appropriate by the commissioners court, including an obligation that is required to be approved by the attorney general under Chapter 1202, Government Code. If the obligation is in a form that must be approved by the attorney general, the obligation must be submitted to the attorney general for approval.

The maximum term of a Contractual Obligation is 25 years, but the term is tied to the actual expected life of the equipment being financed. No election or publication is required, but the county must comply with applicable bidding requirements to make a purchase using Contractual Obligations.

3. General Obligation Bonds

General Obligation Bonds, sometimes referred to as "G.O. Bonds," are bonds secured by the county's ad valorem taxing power. These bonds are issued after approval at a bond election. G.O. Bonds are best suited for major capital projects where the commissioners court believes that it is important to allow the voters to have the opportunity to pass upon the project. The commissioners court calls a bond election, and sets forth the proposition or propositions to be voted on. An amount is specified for each proposition. Costs of issuance of the bonds are included as a part of the issue. G.O. Bonds are sold for cash.

If the election passes, the county must use the proceeds from the sale of the bonds for the purposes stated in each proposition. The amount approved for one proposition cannot be assigned to any other proposition, even if there are excess funds available. Expenditures must be strictly in accordance with what the voters approved. Surplus funds must be placed in the interest and sinking fund and used to pay debt service.

Once the bond election has occurred and the time for any election contest has passed, the commissioners court will place the matter on the agenda, and approve an order authorizing the sale of the G.O. Bonds.

The maturity of bonds should be such that they mirror the useful life of the bonds. G.O. Bonds may be amortized over a 40 year period, although market conditions usually dictate a shorter period of 15 to 20 years.

Bid Requirements

In addition to the requirement that the proceeds of the bonds be spent in accordance with the particular proposition approved by the voters, the county is required to spend the proceeds in accordance with the County Purchasing Act. Section 262.023, Texas Local Government Code provides that the county will spend proceeds of a G.O. Bond by (1) complying with the competitive bidding or competitive proposal procedures of the County Purchasing Act; (2) using the reverse auction procedure, as defined by Section 2155.062(d), Texas Government Code, for purchasing; or (3) complying with the alternative procurement methods authorized by Chapter 2267, Texas Government Code,[4] for construction projects.

Because of the complexity of calling a bond election, a separate chapter is included on Bond Elections.

4. Lease Purchase Obligations

Lease purchase financing can be an efficient, convenient and effective financing tool for counties. Lease purchase financing can be used for both equipment acquisition and real property transactions. It is important to analyze the reason for the lease purchase. The consequences of the acquisition of a new computer and the acquisition of a new jail may be quite different.

Lease Purchase Agreements that are not secured by a debt obligation are not required to be submitted to the Attorney General for approval, but they may be submitted at the option of the county. If the Lease Purchase Agreement is divided into separate

[4] For counties, this was formerly found in Subchapter H of Chapter 271, Texas Local Government Code.

securities known as certificates of participation, the certificates of participation must be submitted to the attorney general for review and approval.

It is important to determine whether the lease is simply a salesman's proposal or a well thought out financing in which the county considered all the alternatives. Generally, your bond counsel or financial advisor will be glad to review the proposal and provide advice on the transaction. Most will do this without additional cost to the county, as a part of their ongoing relationship.

Equipment Financing

Lease purchase financing has become a very efficient and economical method of acquiring equipment and other personal property. Some of the interest rates offered by vendors with their financing programs are very competitive, but sometimes on a comparable basis to the rate a county could obtain through the issuance of Tax Notes or Contractual Obligations. Unfortunately, some lease agreements will have rates in excess of what the county could obtain if it did a conventional financing. For the acquisition of a single piece of office equipment, the lease purchase method may be the best method to use. However, it is important to determine what the interest rate actually is. If it is out of line with the rate for a conventional financing, the county should question the rate and if an appropriate rate is not offered, contact other vendors.

A county considering a lease purchase arrangement should make an apples-to-apples comparison to determine the cost of the lease purchase arrangement to that of other forms of financing. First, get the vendor to provide the cost for the item with lease purchase financing and the cost if the county paid cash. While a small equipment lease purchase transaction can be very efficient, it may be less expensive to do a conventional financing transaction for a larger purchase. If in doubt, contact your bond counsel and financial advisor for assistance.

Real Property

With the exception of certain equipment lease purchase arrangements that are structured in compliance with the Public Property Financing Act, Subchapter A of Chapter 271 of the Texas Local Government Code, lease purchase transactions are paid from an annual appropriation from the county's maintenance and operations tax, and are not treated as ad valorem tax debt. Therefore, they go on the maintenance and operations side of the truth in taxation calculation, not the interest and sinking fund debt side. Consequently, these transactions will be subject to roll back, whereas a valid debt obligation is not.

When a county uses a lease purchase transaction for a real estate transaction, it will generally pay a substantially higher amount in costs of issuance. In addition, a developer usually puts together the lease purchase transaction. The developer will arrange for and supervise the construction of the facility. Consequently, there will be a substantial developer's fee included in the financing.

The attractiveness of using lease purchase financing for a real estate project will require the county to examine whether it would be more appropriate to use traditional financing. An area where the lease purchase method is often promoted is for a county jail or correctional facility. Generally in these transactions, a public facility corporation is created under Chapter 303, Texas Local Government Code, to insulate the county from potential financial exposure. In a jail financing, the concept is that the facility will be paid for primarily through housing out-of-county prisoners for a fee. While this is possible, the county must explore how firm the supply of prisoners will be. To the extent the county does not have sufficient income from housing out-of-county prisoners, the county will be responsible for making up the difference. Should the county choose to exercise its right to not appropriate funds, there are several consequences. First, the county may have to contract with another county to house its own prisoners. Second, while the county may not be obligated for payments once it exercises its right not to appropriate, rating agencies may downgrade the county's bond rating. It is important to fully understand what is involved in the transaction.

Lease Purchase Transaction Must be Properly Structured

Care must be taken to ensure that the lease purchase arrangement is a valid obligation. Unless structured as a debt under the Public Property Financing Act, the lease must provide that the obligation is to be paid from available revenues and that the county may cease to appropriate funds and discontinue the obligation at any time. Some Lease Purchase Agreements contain provisions that violate the Constitution, such as in *City-County Solid Waste Control Board v. Capital City Leasing, Inc.*, 813 S.W.2d 705 (Tex. App.--Austin 1991, writ denied), where the court found a Lease Purchase Agreement for certain machinery constituted an illegal attempt to create a debt and voided the agreement.

Lease Documents Need to be Reviewed and Negotiated

Today, many equipment vendors, both high-tech and heavy equipment, utilize very well written leases that comply with Texas law. They contain subject to appropriation provisions. Unfortunately, there are still some lease document forms that are not properly written. Most Lease Purchase Agreements are presented by vendors. The documents are preprinted, so that the county only has to pass an order to authorize the issue. Very often the county attorney is asked to give an opinion, including the federal tax-exempt status of the transaction. It is important to remember that the lease provisions can be negotiated. Very often lease purchase transactions will provide for a very competitive interest rate; sometimes they do not. A county should consider having the documents and interest rate structure reviewed by its bond counsel to see if the transaction is properly structured and by its financial advisor to see if the interest rate is appropriate. It may be that the financing can be done as a traditional financing in a more cost effective manner. Sometimes it may not, but it is worth checking.

The County Must Be Prepared to Terminate

The county needs to consider two primary questions before using Lease Purchase Agreements: Will the county have adequate revenues to make the payments? And, will a maintenance and operations tax increase be required, and if so, will it trigger a rollback election? The answer to these questions, for jail financing in particular, is important. If the jail is to hold the county's own prisoners, it is important to understand how the lease payments will be funded. Unless there is a revenue stream from housing prisoners from other jurisdictions, payments will come from the county's maintenance and operations tax, not its debt service tax. Will the county be able to keep up the payments if the county's economic situation takes a down turn? What will the county have to cut in order to maintain the payments if there is a successful rollback election?

5. Refunding Bonds

Refunding Bonds are authorized under Chapter 1207, Texas Government Code. Refunding Bonds are issued by a county to refinance its outstanding bonds by issuing new bonds. Refunding Bonds are generally issued to reduce the county's interest cost by issuing the new bonds at a lower interest rate. Refunding Bonds may also be issued to restructure a county's debt service requirements.

Historically, Refunding Bonds have been either issued as a current refunding or an advance refunding. A current refunding is where the outstanding bonds being refunded are taken out of the market within 90 days of the closing on the new Refunding Bonds. An advance refunding is where an escrow fund is established to take out the outstanding bonds at a date in excess of 90 days. In either case, the outstanding bonds will be taken out at their call date which is set forth in the order which authorized the outstanding bonds. Refunding Bonds do not require an election or newspaper publication.

As a consequence of the Tax Cuts & Jobs Act of 2017, tax-exempt advance refundings are no longer authorized for the refunding of local government bonds. As such, counties wishing to issue tax-exempt refunding bonds must take care to structure the transaction so that the refunding is accomplished within 90 days of closing. It should be noted that under certain circumstances, a county may issue a taxable bond for an advanced refunding transaction.

The county's financial advisor will determine how best to sell the refunding bonds. This may be done at a regular meeting where all details have been worked out, including the purchaser, the amount of bonds to be refunded, and the par amount of the bonds to be sold. The commissioners court approves the order resulting in the sale of the bonds and the refunding of the prior bonds or other obligations. Chapter 1207 also provides for the commissioners court to approve the refunding bond order by specifying certain parameters: the bonds that can be considered for refunding, the maximum principal amount that can be issued, the maximum interest rates for the refunding bonds and the minimum savings that must be produced by the refunding. The commissioners court approves the order authorizing the bonds with certain information not completed, and delegates the authority to complete the sale to one or more county officials who will serve as a pricing officer. The financial advisor will then attempt to arrange for the sale of the refunding bonds in a way that will meet the parameters established by the commissioners court. If the parameters are met, the pricing officer will approve the sale by issuing a pricing certificate which completes the missing information.

Refunding Bonds are submitted to the attorney general for approval. The obligations being refunded must have been validly issued. If not, the county will have to have the obligation validated as a valid debt under Chapter 1205, Texas Government Code.

In addition to refunding the county's outstanding debt instruments like G.O. Bonds, CO's, and Tax Notes, Refunding Bonds may also be used for any general or special obligation. An example of this type of obligation would be a judgment. If a court approved a million dollar judgment against a county and the county did not have available funds to pay the judgment, the county could issue Refunding Bonds to pay the judgment.

6. Public Facility Corporation Lease-Purchase Obligation

Counties are authorized to create entities known as "Public Facilities Corporations" that will issue debt for the acquisition, construction, rehabilitation, renovation, and equipping of public facilities. When such a corporation is used to finance a county project, the corporation will own the improvement and the underlying land and then lease the land and improvement to the county with an option to purchase. The "rent" paid by the county to the corporation is used to pay the debt service on the bonds issued by the corporation. The primary benefit of using this type of financing structure for the county is that the debt obligation belongs to the corporation, not the county.

7. Revenue Bonds

Revenue Bonds, unlike general obligation bonds, do not involve an ad valorem tax pledge. Revenue bonds are secured by the pledge of revenues of a project of the issuer. These bonds are not subject to a demand for payment from taxes. No election is required under State law to issue revenue bonds. Most counties generally do not have projects which will support revenue bonds, although some do. If a sufficient revenue stream exists, revenue bonds could be issued, secured by, for example, water systems, toll roads or parks.

The county will be required to set rates that will cover debt service for the bonds being issued and any outstanding bonds, as well as the costs of maintenance and operation of the system producing the revenues. There usually will be a requirement that the county will maintain a debt service coverage ratio, usually 1.10 to 1.25 times the required debt service. Most revenue bonds involve a pledge of net revenues, that is, revenues that are available after the operational expenses of operating the system or project have been deducted. The county will also establish a reserve fund. Often, the county will be required to enter into a trust indenture with a bank so that the revenues are placed in a trust account to pay debt service.

A public improvement district bond is a revenue bond that is paid by assessments levied against property in the district. This type of revenue bond is discussed in more detail in Section VII.C.2.

8. Tax Notes

Tax Notes are the most recent addition to the financing options available to counties. They were authorized by the legislature in 1993. The provisions governing Tax Notes are found in Chapter 1431, TEX. GOV'T CODE. Technically, these notes are called "Anticipation Notes" and can be secured by either a pledge of ad valorem taxes or revenues, or both. In order to pledge revenues, there must be specific authority to permit the particular revenue source to be pledged for bonds or similar obligations.

Tax notes have proven to be an effective method for funding capital expenditures in light of current limitations on increases to the maintenance and operations tax.

The issuance process is very streamlined. There is no election or publication requirement. Since few counties have enterprise funds that generate sufficient revenues to finance a project, ad valorem taxes are the primary method of financing using anticipation notes. Consequently, the term "Tax Note" is commonly used to describe this method of financing.

Tax Notes may be issued to:

a. Pay for construction of a public work.

b. Pay for purchase of materials, supplies, equipment, machinery, buildings, lands, and rights-of-way for the issuer's authorized needs and purposes.

c. Pay for professional services such as engineers, architects, attorneys, and financial advisors.

d. Pay for operating expenses or current expenses.

e. Fund the issuer's cumulative cash flow deficit.

Tax Notes have a short maturity which may not exceed seven years from the date of the attorney general's approval for Notes issued for capital improvements. Tax Notes can also be issued to pay operating expenses or to fund a cash flow deficit and Tax Notes issued for these purposes may not exceed one year from the date of the attorney general's approval. Additional restrictions are imposed on the percent of revenues or taxes pledged for Notes issued to pay operating or current expenses.[5]

In order to issue Tax Notes, the County Auditor must recommend issuance. For counties that do not have a county auditor, the county judge, as the county budget officer, is required to make the recommendation. Section 1431.002(a), TEX. GOV'T CODE.

There are procurement restrictions on using Anticipation Notes for construction projects. First, in order to use proceeds from Anticipation Notes for construction projects, the county must comply with the competitive procurement requirements of the Certificate of Obligation Act. Section 1431.012 provides:

§ 1431.012. Restriction on Certain Contracts Payable From Proceeds of

[5] A note issued by an issuer participating in the economic development program established by the Texas Agricultural Finance Authority may have a maturity of up to thirty years. Such notes are limited to a principal amount not to exceed $500,000.

Notes

(a) Except as provided by Subsection (b), a county must comply with the competitive bidding requirements of Subchapter C, Chapter 271, Local Government Code, in connection with a contract to be paid from the proceeds of anticipation notes issued for a purpose described by Section 1431.004(a)(1)(A).[6]

(b) Competitive bidding requirements do not apply to an anticipation note or other obligation issued under Section 1431.015[7] for any authorized purpose.

Originally, a county could refund a Tax Note which would mature within seven years of its dated date. The legislature amended Section 1431.009, TEX. GOV'T CODE, to permit refunding up to forty years from its dated date.

9. Time Warrants

Time Warrants are one of the oldest and most misunderstood obligations that a county can issue. They are backed by the county's ad valorem tax. Unlike G.O. Bonds, CO's, Tax Notes and Contractual Obligations, Time Warrants are not negotiable instruments. Time Warrants are authorized for counties under Chapter 262 of the Texas

[6] Section 1431.004(a)(1)(A) addresses the "construction of a public work."

[7] In response to Hurricane Rita, Section 1431.015, TEX. GOV'T CODE, was added to exempt certain emergency financings from the competitive bid requirement where (1) the governor has issued an emergency proclamation declaring a state of disaster and designating a disaster area under Chapter 418, TEX. GOV'T CODE; (2) the governing body of the issuer (commissioners court) has declared a local state of disaster designating the area affected by the emergency under Chapter 418, TEX GOV'T CODE; or (3) the governor has proclaimed a state of disaster and designated an affected area under Chapter 433, TEX. GOV'T CODE. In such instances, the Attorney General's review process is expedited. Tax Notes issued pursuant to Section 1431.015 must mature within 10 years of the approval by the Attorney General.

Local Government Code.[8] They are expressly exempt from the requirement of attorney general approval and comptroller registration by Section 1207.007, Texas Government Code.

A Time Warrant is defined as "... any warrant issued by a county that is not payable out of current funds." Section 262.0022(9), Texas Local Government Code. Time Warrants are subject to the same publication requirements and voter petition/election requirements as CO's, but may not be sold for cash. The vendor can then attempt to sell the warrant to a bank or other purchaser. These requirements are seen in Section 262.025, Texas Local Government Code:

> (a) A notice of a proposed purchase must be published at least once a week in a newspaper of general circulation in the county, with the first day of publication occurring before the 14th day before the date of the bid opening. If there is no newspaper of general circulation in the county, the notice must be posted in a prominent place in the courthouse for 14 days before the date of the bid opening.
>
> (b) The notice must include:
>
> (1) the specifications describing the item to be purchased or a statement of where the specifications may be obtained;
>
> (2) the time and place for receiving and opening

[8] A word of caution. Other statutory procedures exist for issuing time warrants for specific situations, such as Section 1477.152, Texas Government Code, for the purchase of firefighting equipment. If used, those provisions must be reviewed carefully to ensure that all special requirements are complied with.

bids and the name and position of the county official or employee to whom the bids are to be sent;

(3) whether the bidder should use lump-sum or unit pricing;

(4) the method of payment by the county; and

(5) the type of bond required by the bidder.

> (c) ***If any part of the payment for a proposed purchase will be made through time warrants, the notice also must include a statement of the maximum amount of time warrant indebtedness, the rate of interest on the time warrants, and the maximum maturity date of the time warrants.***

(Emphasis added). The election requirement will arise if a valid petition is presented. Section 262.029, Texas Local Government Code provides:

> If before the date tentatively set for the authorization of the issuance of time warrants applying to a contract covered by this subchapter or if before that authorization a petition signed by at least five percent of the registered voters of the county is filed with the county clerk protesting the issuance of the time warrants, the county may not issue the time warrants unless the issuance is approved at an election ordered and conducted in the manner provided for county bond elections under Chapter 1251, Government Code.

These requirements may come as a surprise in that many counties have traditionally sold Time Warrants to a local bank to finance a purchase. Time Warrants must be delivered to the vendor in exchange for the purchase. In some instances, where a county delivered a time warrant to a bank, the bank has treated the Time Warrant as being a tax-exempt obligation. Under federal tax law, only obligations that are properly issued under State law are entitled to have interest treated as tax-exempt. If Time Warrants are used, the county should attempt to make arrangements with a local bank to agree to purchase the Time Warrant from the vendor. In that instance, the county could issue the Time Warrant to the vendor, and the vendor would be able to assign the Time Warrant to the bank.

Historically, counties used to fund many purchases through Time Warrants issued to vendors. The county would then accumulate a number of warrants and refund them through the issuance of a Refunding Bond, which is a negotiable instrument. Time Warrants are not required to be submitted and approved by the attorney general. However, if the county wants to refund Time Warrants into a Refunding Bond, the Refunding Bond must be submitted and approved by the attorney general. In order to refund a Time Warrant, it must have been validly issued. So if the county did not comply with the notice and publication requirements, the Time Warrant cannot be refunded unless it has been validated through a bond validation lawsuit.

Time Warrants are treated the same as G.O. Bonds in regard to the bidding requirements of the County Purchasing Act, including the use of the alternative procurement provisions of Chapter 2267, Texas Government Code.

C. Charts Summarizing Authorized Purposes and Relevant Instruments

The following charts are intended to be useful for quick reference. The first chart shows what debt instruments may be available for use by a county depending on the purpose of the financing. The second chart summarizes the key features of each debt instrument.

Table I
Authorized Purposes for Issuing Debt Obligations and Related Debt Instrument Types

General Purposes	Form of Debt/Debt Instrument Type
• Acquisition of real property • Construction of public improvements (including roads) • Renovation • Public improvement/works • Development-related professional services	• Certificates of Obligation • General Obligation Bonds • Public Facility Corporation Bonds • Revenue Bonds (including Road Utility Districts, Public Improvement Districts, and Transportation Improvement Zones) • Tax Notes
Cash-flow deficit financing and current expenses	• Tax Notes
Personal property	• Contractual obligations (e.g., lease, lease with option to purchase, installment purchase) • General Obligation Bonds • Time Warrants

Table II
Defining Features of the Different Authorized Forms of Obligation

Instrument/Obligation Type	Statutory Source	Obligation Characteristics
Certificates of Obligation	Chapter 271 Local Government Code, Subchapter C	• May be used for construction; materials, equipment and machinery; buildings, land and right of way;

Instrument/Obligation Type	Statutory Source	Obligation Characteristics
		and professional services. • No election required if there is no valid petition protesting the issuance. • Payable from ad valorem taxes, revenues, or a combination. • Uses of proceeds are more limited if the repayment is by taxes only.
Contractual Obligations	Chapter 271 Local Government Code, Subchapter A	• May be used to finance personal property. • May be in the form of lease, lease with option to purchase, installment purchase, or other form. • Depending on form, it may require attorney general approval.
General Obligation Bonds	Chapter 1251 Texas Government Code	• May be used for any legitimate county purpose that is approved by the voters. • Secured by ad valorem taxing power. • Requires an election. • Best suited for large projects where Court believes voters should be able to pass on the project.

Instrument/Obligation Type	Statutory Source	Obligation Characteristics
Public Facility Corporation Lease-Purchase Obligation	Chapter 303 Texas Local Government Code	• May be used for acquisition, construction, rehabilitation, renovation, and equipping of public facilities. • The county creates a Public Facility Corporation (PFC) to issue the debt and to develop the improvement. • The improvement is leased to the County with an option to purchase. The "rent" paid by the County is applied to debt service. • This structure insulates the county from potential finance exposure because the debt belongs to the PFC, not the county.
Refunding Bonds	Chapter 1207 Texas Government Code	• These are issued to refund outstanding bonds, typically to obtain more favorable debt-service terms. • Must be used to refund bonds within 90 days of issuance. • Court can authorize bonds to be sold subject

Instrument/Obligation Type	Statutory Source	Obligation Characteristics
		to parameters rather than specific terms to allow Financial Advisor to find best price in the market.
Revenue Bonds	Various places, including: • Chapter 320 Texas Local Government Code, Subchapter D (Parks) • Chapter 372 Texas Local Government Code (Public Improvement Districts) • Chapter 563 Texas Local Government Code, Subchapter C (Water and Wastewater) • Chapter 1479 Texas Government Code (Highways)	• May be used for statutorily limited purposes including parks, public improvement district improvements, water and wastewater, and highways and roads. • Do not require ad valorem tax pledge. • No election is required. • Typically require debt service reserve fund with a coverage ratio of 1.10 to 1.25 annual debt service.
Tax Notes (aka "Anticipation Notes")	Chapter 1431 Texas Government Code	• May be used for construction; materials, equipment and machinery; buildings, land and right of way; professional services; payment of current operating expenses; and funding cash-flow deficits.

Instrument/Obligation Type	Statutory Source	Obligation Characteristics
		• Can be secured by ad valorem taxes, revenue, or a combination. • There is no election or publication requirement. • The repayment period may not exceed seven years. • Must have County Auditor's recommendation.
Time Warrants	Chapter 262 Texas Local Government Code	• May be used for purchase of items covered by Chapter 262 Texas Local Government Code, Subchapter C. • Not negotiable instruments. • Attorney general approval is not required. • They are used as payment to a vendor and the vendor, not the county, sells the warrant to a bank for cash or another purchaser.

III. Overview of the Process for Issuing Bonds, Certificates of Obligation, and Tax Notes

Key Points

- *In planning to issue debt, a county will need to consider the entire scope of the project to be funded, the timing involved in issuing debt, and methods for ensuring compliance with federal and state requirements after the debt has been sold.*
- *The issuance of debt requires the coordinated effort of the county, its consultants, the state government, and others.*
- *This section of the handbook describes the process for issuing debt, the roles of some of the professionals involved in the issuance of debt, and the general timeline that applies to certificates of obligation, general obligation bonds, and tax notes.*

A. General Process

1. The Financing Program Should Account for the Entire Project

A county should not focus on the issuance of bonds as a separate process from the project to be financed. It is important to keep the entire project in perspective. First, it is important to get a good estimate for the cost of the project. The estimates for the project need to be reviewed and challenged to ensure that the amount projected will actually be sufficient to complete the project. For equipment and materials, the persons in charge of county purchasing will need to obtain cost estimates of the items to be purchased in order to determine the amount of bonds to be issued. For construction projects, the county will need to engage design professionals, such as architects and engineers, to provide the initial cost estimate on which the amount of bonds will be based. For instance, when a county is planning a new jail project, it will need an architect experienced in jail design to provide an estimate of the construction costs in order to properly size a bond issue. A major concern is that the estimate may be low. This can result in either reducing the size of the project or issuing additional debt to complete the project. When a county has represented to the public the cost of a project, it certainly does not want to have to issue additional bonds to finish the project.

It is important to keep preliminary costs in perspective. While the bond counsel and the financial advisor work on a contingent basis, architects, engineers and others do not. A county should provide protection in its contracts with design professionals in the event the financing does not go forward. Why would a project not go forward? If a bond election is used, it is possible that the bonds may not pass. Circumstances may change where the project is no longer needed. For contracts with architects, the county should consider establishing preliminary dollar limits, beyond which it will have no responsibility if the project does not go forward. The contract should provide for a preliminary phase where the architect will provide a cost estimate for a fixed amount so that this will be the limit of compensation if the financing does not go forward. Unless a county is willing to pay for work that may not be needed, the architect should not be permitted to complete the design phase until the financing has been completed.

Also, the county should consider **NOT** using the traditional AIA contracts for architect or construction. If an AIA contract is used, you should negotiate the terms so that the county is on a more equal basis. (AIA Contracts are discussed in more detail in Article VII of this Handbook, below). The county is about to spend a lot of money on a bond project; make sure the county is protected. Finally, if the bonds are for a construction project, make certain that the performance and payment bonds are properly written and in place before funds are released to a contractor.

2. Order of Events and Key Considerations

The general order of events in the issuance of debt is as follows:

- The county consults with its financial advisor and, or, bond counsel to determine the most efficient plan of finance for the project under consideration.
- The bond counsel, in coordination with the county and the financial advisor, drafts the documents needed to obtain the commissioners court's authorization and to complete the transaction. (The key documents are discussed in Section III. D. of this handbook, below.)
- The court authorizes the issuance of debt.
- The debt sale transaction closes and funds are wired to the county's project account.
- The county monitors its compliance with tax and securities requirements until the debt is retired.

The following points might influence the process for the issuance of debt, depending on the instrument used:

- If the county chooses to issue certificates of obligation, the commissioners court will need to approve the publication of notice of the intent to issue certificates of obligation. The notice must be published once a week for two consecutive weeks in a local newspaper of general circulation in the county, before the meeting at which the court authorizes the sale of the certificates of obligation. (Tex. Loc. Gov't Code § 271.049).
- The Texas Constitution requires counties to levy a tax in an amount sufficient to pay the interest on the debt and to create a sinking fund of at least two percent of the debt. (Tex. Const. Art. XI § 7, a copy of which provision is attached as Tab 3).
- A county will need to approve the order to issue the bonds or other tax-backed obligations at a regularly scheduled meeting of the commissioners court. The order authorizing the bonds is also the order authorizing the sale and the levy of the tax to support debt service on the bonds. A tax may not be levied unless at least four members of the court are present and at least three members of the court vote in favor of the levy. (Tex. Loc. Gov't Code § 81.006).
- If the county needs to proceed with the project before the financing can be complete, it may want to pass a **reimbursement resolution** to permit the county to use available funds which it will reimburse from the sale of the bonds later. If the funds needed are only for preliminary work, such as professional expenses for architectural and engineering expenses, those expenses can be reimbursed without a formal reimbursement resolution. If a construction project is involved, the breaking of ground will be considered a construction cost rather than a preliminary expenditure. Depending on the debt instrument used, the resolution may need to comply with federal tax requirements.

B. Consultants and Other Persons Involved

The following is a roster of the key participants in the typical issuance of county debt:

Attorney General of Texas – The attorney general reviews and approves certain securities that are issued by counties and other Texas political subdivisions. The attorney general's approval is in the form of a written opinion. State law prescribes that the county (and other issuers) pay a fee equal to 1/10th of 1% of the par value of the bonds, subject to a $750 minimum and a $9,500 maximum fee, for the review of the securities **transcript** (defined in Section III. D. of this handbook, below).

Bond Counsel – Bond counsel is an attorney retained by the county to assist in the issuance of the bonds. Bond counsel will prepare the documents needed to issue the bonds or other security (including resolutions and the bond order), submit the transcript of bond proceedings to the Attorney General of Texas for approval, assist in the closing, and deliver an opinion that the county is authorized to issue the bonds, that the county has met all legal requirements for the issuance and that the interest on the obligations will be exempt from federal income taxation. If there is a bond election, bond counsel will prepare the bond election materials. A county has the right to choose its own bond counsel. It is advisable that the county select a bond counsel that is listed in the *BOND BUYERS' MUNICIPAL MARKETPLACE* (commonly known as the "Red Book"), which lists law firms which are recognized as having served as bond counsel or underwriters counsel.

Bond Insurers – Bond insurers provide insurance policies to ensure payment of principal and interest on the securities in the event the county becomes unable to do so. When a county obtains bond insurance, the county's bonds take on and carry the credit rating of the insurance company. Bond insurance may only be used if the county will receive the benefit of a lower overall debt service on the bonds after the cost of the bond insurance premium is considered.

Comptroller of Public Accounts of Texas – The comptroller registers the county's bonds after they have been approved by the attorney general.

Credit Rating Agencies – The three major credit rating agencies for county bonds are S&P Global Ratings, Moody's Investors Services, and Fitch Ratings. These agencies, if engaged by the county, will rate the financial condition of the county and its ability to repay the bonds. Investors use the ratings in determining the risk of their investment. Investors will look to see if the bonds are rated as being investment grade, a credit designation given municipal securities that have a high rate of probability of being paid.

Depository Trust & Clearing Corporation (DTCC) – The DTCC serves as the depository for the securities and also provides settlement services. DTCC holds the securities for its participants, who are the individuals and entities that purchase the bonds (the depository function). DTCC accepts the county's payment of debt service and ensures that each participant receives its proper portion of that payment (the settlement function).

Financial Advisor – The financial advisor is a person or firm who advises the county on securities offerings. Each individual financial advisor is required to have a securities license; their activities are regulated by state, federal and industry securities regulatory authorities. The financial advisor will advise the county on the type of security to issue (such as general obligation bonds, certificates of obligation or tax notes), how to structure the issue, and how the bonds will be sold, i.e., through a **competitive sale** – through bids which will determine the price and the interest rates at which the bonds are sold; a **negotiated sale** – where the interest rates and purchase price are negotiated with an underwriter; or a **private placement** – where the bonds are sold directly to a local bank. The financial advisor will determine how best to position the county for the market, including whether to sell the bonds with bond insurance and whether to have the bonds rated by one or more of the rating agencies.

Internal Revenue Service – The Internal Revenue Service is the federal entity which issues and enforces rules regarding the tax-exempt status of bonds.

Paying Agent – The paying agent is a commercial bank that handles the closing of the bonds, registers the owners of the bonds and coordinates the receipt of debt service payments from the county and the payment to the owners of the bonds.

Securities and Exchange Commission – The Securities and Exchange Commission is the federal entity that issues and enforces rules regarding the disclosure of information pertaining to securities issued by a county.

Underwriter or Purchaser – The underwriter is the entity that makes the initial purchase of a county's securities that are sold through either a competitive sale or a negotiated sale for the purpose of reselling all or a portion of those securities to other investors. For most transactions the underwriter will be a brokerage firm or bond dealer or a syndicate of two or more firms. In a private placement transaction, the purchaser is the bank, entity, or individual who purchases the obligations direction from the county.

C. Timelines

Timing is a critical element of the county's financing plan. The following chart shows some of the general differences in timing between funding with general obligation bonds, certificates of obligation, and tax notes.

Timing Comparison

	General Obligation Bonds	Certificates of Obligation	Tax Notes
Time Involved Before Funding	Five to 12 months	45-60 days	30-45 days
Election/Publication Requirements	Election required The election must be called for May or November on a uniform election date at least 78-90 days before the elections	County must authorize the publication of the notice of intent to issue the certificates, with the first publication at least 45 days before authorization	None
	Canvass election		
	If the election passes, place the item for authorization of the bonds on the regular meeting agenda 30 days after canvassing	If there is no petition that challenges the issuance, place the item for authorization of the sale on agenda for regular meeting	Place the item for authorization of sale on agenda for regular meeting
	Funding completed within 30 days from sale date	Funding completed within 30 days from sale date	Funding completed within 30 days from sale date

D. <u>Attorney General Review and Approval after Commissioners Court's Authorization</u>

The Texas Public Securities Procedures Act establishes a process by which most[9] "**public securities"** are approved by the attorney general and registered with the comptroller before they are issued. Attorney general review typically occurs after the county has approved the sale of the securities. In some instances, when the project schedule requires it, the securities can be submitted to the attorney general for consideration before the court has authorized the sale.

As discussed below, the purpose for the approval and registration requirements is to establish that such approved and registered securities are valid and incontestable in the face of any legal challenges. The approval and registration requirement, then, provides comfort for the purchasers of securities in that the repayment of the principal and interest, if any, is a legal obligation that is binding on the seller of the bonds. Approval and registration also provides comfort for the issuer of the bonds in that the financing structure for its project is valid.

The Texas Public Securities Procedures Act defines a "public security" as "an <u>instrument</u>, including a bond, certificate, note, or other type of <u>obligation</u> <u>authorized to be issued</u> by an issuer under a statute, a municipal home-rule charter, or the constitution of this state" Tex. Gov't Code §1201.002(2) (underline added).

Some of the key features of this statutory definition include its use of the terms "<u>instrument</u>" and "<u>obligation</u>," as well as the phrase "<u>authorized to be issued</u>." Taking the terms out of order, "obligation" here means a legal obligation of the issuer, who for

[9] Time warrants and certain forms of contractual obligations do not need to be approved by the Attorney General in the same manner as "public securities."

our purposes will be a Texas county, to repay a certain amount of money to a lender, or to a trustee or paying agent representing a group of lenders. These obligations are debts, as that term is used in this handbook. "Instrument" here means a written document that evidences the *obligation* to repay a certain amount, plus interest, and at certain times and under specific conditions. And the phrase "authorized to be issued" is used to indicate that an issuer may only issue debt when it has specific authority to do so. The statutory definition then is a restatement of the fundamental principal that a county may not issue an obligation that cannot be repaid out of funds available to it in the current budget, unless it has express statutory or constitutional authority.

As stated, most public securities, and the "record of proceedings" relating to the securities, must be submitted to the attorney general for review and approval, before they are issued. (Chapter 1202 Texas Government Code). Please note that the "record of proceedings," for the purposes of this handbook, will be referred to as a "**transcript**." For a typical county security transaction, the county must submit the transcript to the attorney general for review *at least 14 days prior* to the scheduled closing for the sale of the securities. (See, 1 Tex. Admin. Code §53.16(b)).

When the attorney general reviews a public security and the related transcript, the attorney general is verifying that the county has the requisite statutory or constitutional authority to issue the security, that the security has been approved in accordance with the applicable procedures, and that the form of the security includes all of the terms required by State law.

1. Essential Transaction Documents

The exact requirements for each transcript will vary from transaction to transaction depending of the type of public security being issued. The essential documents that apply to all public security transactions that are subject to attorney general review are listed in Title One of the Texas Administrative Code at Section 53.3. Below is a brief description of some of the most commonly required transcript documents. The following list is not exhaustive. It is intended to give the reader a sense of the types of material that the attorney general requires to confirm the validity of a public security.

Authorizing Document – This is the order of the commissioners court that approves the issuance of the securities. The order must contain the terms specified in §53.3(a) (2). The required terms include a description of the securities by reference to the date, denominations, payment dates and amounts, and redemption terms. The order must also reference the constitutional or statutory authority for the issuance of the obligation and the source of repayment. The order also must state the manner in which the security will be sold, the identity of the purchaser, the purchase price, and a description of the project to be funded. The order typically identifies which county representatives are authorized to sign various transcript documents. (1 Tex. Admin. Code §53.3(2)).

Acknowledgement of Special Meeting – If the order is authorized at a special meeting, any commissioner that did not attend the meeting must sign an acknowledgement affirming that the commissioner had adequate notice of the meeting. (1 Tex. Admin. Code §53.3(11)).

Certification of Official Actions – This document is typically signed by the county clerk. For each official action taken by the court in connection with the issuance of the security, the county must provide a signed certificate, which includes a true and correct copy of the action taken, stating that a quorum was present, the type of meeting (i.e., regular, special, or emergency), and a tally of votes for and against, and abstentions. (1 Tex. Admin. Code §53.3(12)).

Signature Identification and No-Litigation Certificate – This document is typically signed by the Judge and the County Clerk, and is notarized. The certificate must be submitted to the attorney general undated. The certificate must include certification that no litigation is pending or threatened against the county that seeks to restrain or enjoin the issuance of the securities, or that otherwise questions the authority of the county to issue the securities. The certificate must also certify that no litigation is pending or threatened against the county that would materially affect the county's ability to pay the principal and interest on the obligation, or the county's ability to assess or collect taxes as required to pay the debt service. Also, the certificate must certify that the right to hold office of any commissioner, or any other elected or appointed official of the county, is not being contested. (1 Tex. Admin. Code §53.3(13)).

Affidavit of Publication – If the issuance of the obligation is required to be approved at a public hearing, notice of the hearing must be given in a newspaper that meets state law requirements in terms of volume of distribution within the county. A representative of the newspaper that published the notification of the hearing must sign an affidavit establishing that the newspaper meets the state requirements and that the newspaper published the notice on the relevant dates. Copies of the notice must be attached to the affidavit.

Election Proceedings – If the securities have been authorized by an election, certified copies of the election proceedings must be included as part of the transcript. (1 Tex. Admin. Code §53.3)(16)).

General Certificate – This document typically is signed by the judge and county clerk. The certificate includes a debt service schedule and a statement as to the amount of the required sinking fund, if any. The certificate also includes affirmation of the incumbency of the county officers signing the certificate. The actual content required for the certificate varies depending on the issuer and the type of security. (See, 1 Tex. Admin. Code §53.03)(4)).

Offering Document – This is a document prepared by the county to market the obligations to potential investors. Depending on the type of sale, this document can be a private placement letter or memorandum, a limited offering memorandum, or an official statement. The final version of the document must be included in the transcript.

Bid Form – If the sale of the obligation is a **competitive sale**, the transcript requires a copy of the winning bid form. (See, 1 Tex. Admin. Code §53.03(6)).

Pricing Certificate – This document typically is signed by the county auditor. Certain securities require a pricing certificate to establish the price of the sale of the securities. The price as stated in the certificate is needed to verify compliance with federal tax laws relating to **arbitrage**, which is discussed in a separate section of this handbook. If the securities were sold subject to parameters specified in the order, the pricing certificate establishes compliance with those parameters. (See, 1 Tex. Admin. Code §53.3(3)).

Purchase Agreement – This document typically is signed by the county judge. This document is required if the sale of the security is a **negotiated sale**. This document is the agreement between the county and the purchaser of the obligation and includes all the terms required to effectuate a sale. (See, 1 Tex. Admin. Code §53.03(5)).

2. Preliminary Approval

The attorney general typically has ten days from the submission of the transcript to review the transcript and issue a "preliminary approval letter" (the "**P-Letter**"). The attorney general will not, however, unless requested by counsel, issue a P-Letter sooner than the end of the fifth working day before the date set for closing. (1 Tex. Admin. Code §53.16(d)).

The purpose of the P-Letter is to notify bond counsel of any clarifications or additional information that the attorney general needs before it can approve of the sale of the public securities. Bond counsel usually will have phone conversations with the attorney general's office to verify that it understands the issues presented in the P-Letter and then will respond to the P-Letter with written responses and additional documentation as required. (1 Tex. Admin. Code §53.16(d)).

3. Approval

The attorney general, upon receiving the information specified in the P-Letter, will deliver to the county's bond counsel a copy of the attorney general's legal opinion stating approval of the securities. (Tex. Gov't Code §1202.003). The attorney general also forwards a copy of its opinion, and a copy of the transcript, including the security, to the comptroller for registration. (Tex. Gov't Code 1202.005).

4. Validity and Incontestability

The public securities approval and registration procedures, once completed, provide a substantial degree of comfort to the county who issued the securities and the purchasers of those securities, in that once the bonds have been approved, registered, and issued, their validity cannot effectively be challenged. As stated in the Government Code: "A public security and any contract the proceeds of which are pledged to the payment of the public security are valid and incontestable in a court or other forum and are binding obligations for all purposes according to their terms: (1) after the public security is approved by the attorney general and registered by the comptroller; and (2) on issuance of the public security. (Tex. Gov't Code §1202.006(a)).

E. <u>After the Sale / Compliance Considerations</u>

The proceeds from the sale of the securities are deposited with the county account at the closing of the transaction. After closing, there are four (two if the securities are not issued as being tax-exempt) general areas that the county will need to monitor to stay in compliance with applicable finance laws:

1. *The terms of the order* – The order of the commissioners court that authorizes the sale of the debt specifies many of the key details regarding the use and management of the funds. The county is obligated to follow the provisions set out in the order for as long as the securities remain outstanding. A few of the more significant requirements relate to the allowed uses of funds and the management of funds. The order will state the purposes for which the proceeds of the security

may be used. The county is obligated to use the funds only for the purposes stated in the order (which will incorporate the purposes stated in the election proposition, if applicable). The order will also authorize the creation of different accounts and funds for the management of securities proceeds, funds for repayment, and security, if any.

2. *Disclosure obligations* – Also, the order will specify the types of information that the county will be required to provide the purchasers during the term of the securities. This information generally includes the county's financial statements and notice of any significant events that might affect the county's ability to repay the obligation. These obligations are generally referred to as the county's **"disclosure obligations"** or **"disclosure undertakings,"** and are discussed in more detail in a separate section of this handbook. The county's disclosure obligations also may be stated in the securities purchase agreement, the offering documents prepared for the marketing of the securities, or in a separate "**Continuing Disclosure Agreement."** It is very important that the county has a comprehensive understanding of its disclosure obligations. Many counties rely on service providers to prepare and issue any statements required to satisfy their undertakings.

3. *Annual Reporting* – Section 140.008, Texas Local Government Code requires each political subdivision, including counties, to annually compile and report certain financial information in a specific manner as prescribed by that section. The report must include:

   (A) the amount of all authorized debt obligations;

   (B) the principal of all outstanding debt obligations;

(C) the principal amount of each outstanding debt obligation;

(D) the combined principal and interest required to pay all outstanding debt obligations on time and in full; and

(E) the combined principal and interest required to pay each outstanding debt obligation on time and in full.

The amounts required in items (A) – (E) are limited to authorized and outstanding debt obligations secured by ad valorem taxation, expressed as a total amount and as a per capita amount, as well as projected per capita amount as of the last maturity date of the most recent debt obligation. The report is to include an explanation of the payment source for the different types of debt.

The county is also required to report the following information for each debt obligation:

(i) the issued and unissued amount;[10]

(ii) the spent and unspent amount;

(iii) the maturity date; and

(iv) the stated purpose for which the debt obligation was authorized.

The report is to include the current credit rating given by any nationally recognized credit rating organization to the county's debt obligations.

The commissioners court is required to ensure that the county's annual report is made available for inspection by any person and is posted continuously on the

[10] This is the language in Section 140.008. For a debt obligation there is no unissued amount. Presumably this means the authorized, but unissued amount remaining from a voted bond proposition.

county's Internet website until the county posts the next annual report, and that the contact information for the county's main office, including the physical address, the mailing address, the main telephone number, and the e-mail address is continuously posted on its Internet website.

As an alternative to actually providing an annual report, a county may provide to the Texas Comptroller of Public Accounts the information required for the annual report, along with any other information the comptroller may require in the manner prescribed by the comptroller. The comptroller will then post such information on the comptroller's Internet website, where the information will be easily located by searching for the name of the county. If the county maintains an Internet website, it is required to provide a link from its website to the location on the comptroller's Internet website where the county's financial information may be viewed. The comptroller is charged with promulgating rules necessary to implement this function.

A similar alternative is also available for a county with a population of less than 35,000. Rather than providing an annual report, it may provide to the Texas Comptroller of Public Accounts a document which contains the required information, and the comptroller will post the information from the document on the comptroller's Internet website. If the county maintains an Internet website, the county shall include a link on its Internet website to the comptroller's Internet website and the web page where the information may be viewed.

While these requirements may seem daunting at first, much of the required information is assembled by the county's financial advisor each time there is a new debt issue. The county may need to request assistance from its financial advisor and bond counsel to update the information.

4. *Federal tax obligations* – As is discussed in a subsequent section of this handbook, if the securities are issued as tax-exempt securities, the county must take steps to ensure that the proceeds received from the sale of the securities are expended on the underlying project in a timely manner, that the proceeds do not earn "**arbitrage**," or if arbitrage is earned, that the appropriate amounts are "rebated" to the federal government, and that the bonds do not become private activity bonds. Arbitrage, for federal tax purposes, generally is any amount earned on the proceeds, such as interest earned on deposits, that is in excess of the yield of the securities. For example, if the yield on the securities (roughly the interest rate) is 3% and the proceeds of the security are earning 3.3% interest while on deposit, that 0.3% difference is arbitrage. If arbitrage is generated, the county will owe the federal government an amount known as a "**rebate."** The terms "proceeds," "yield," "interest" and "arbitrage" have technical definitions for the purposes of the federal tax regulations. A bond becomes a private activity bond if a certain portion of the proceeds, or the project financed with the bond proceeds, is used to benefit a private business use. Although the tax rules are highly nuanced, counties can be sure to stay in compliance if they follow certain bright-line procedures that are established as the financing is being structured.

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IV. <u>Bond Elections</u>

Key Points

- *The timeline for having an election might impact the project.*
- *The court and county employees must be careful to not engage in political advertising.*
- *This section of the handbook describes the election process, the timeline, and restrictions on political advertising.*

A. <u>The Decision to Have a Bond Election</u>

Certain statutory provisions that authorize the issuance of bonds for a county project require the bonds to be approved at an election. The commissioners court must determine whether to call a bond election or to use another type of obligation which does not require voter approval. There is no hard and fast rule about when a bond election must be used. Some counties have established a dollar limit as a rule of thumb (for example, over $5 million or over $10 million will require an election), depending on the size of the county. Other counties base it on the purpose for which the bonds will be used. If the project is one for which there is an unquestioned need, such as a jail that is about to be closed by the Jail Standards Commission, many counties have used certificates of obligation which only require a vote if the citizens request it. If the project is one where there is a need but may be more discretionary, such as a new exhibition center, a bond election has been viewed as more appropriate.

Several different laws are involved in calling a bond election: Texas Election Code, Texas Local Government Code, Texas Government Code and certain limited provisions of the Federal Voting Rights Act. These will all come into play once the commissioners court has decided to call a bond election.

B. <u>Bond Elections – Special Considerations</u>

The affirmative support of the elected officials, and citizen support, is of critical importance to a successful election.

If a commissioners court decides to call a bond election, it should only do so if the members of the court are ready to support the election. If the court is not willing to mount a campaign to provide information on the measure, it is better not to call the election. Either use another type of financing or do not do the project. Unless the need for the bonds is explained and understood by the voters, the bonds probably will not pass.

It is important for the commissioners court to understand that the use of public funds to advocate for the passage of the bond measure is absolutely prohibited. One way citizens organize support for the passage of bond measures is by establishing a citizens committee to support the bonds. This can be done by either establishing a Specific Purpose Campaign Committee if for a single bond issue or if for multiple issues, a General Purpose Political Committee. The committee will have to file the appropriate campaign finance reports.

Citizen support does not spring up overnight. The county may also want to have an advisory committee established with sufficient time before calling the election and let that committee make recommendations on what projects are needed. Once the advisory committee has made its recommendations, a Specific Purpose Political Committee or a General Purpose Political Committee can take on the work of promoting support for the measure.

The County cannot engage in political advertising.

The County may not use public funds to pay for political advertising supporting or opposing the passage or defeat of the bond measure. It may use public funds to generate and disseminate purely factual information that is accurate and that does not advocate the passage or defeat of an electoral measure. Additionally, the County must ensure that it communicates effectively with the protected minority voting populations in the County, such as the Spanish-speaking community, by providing election materials and information in both Spanish and English, when applicable.

It is reasonable to expect that the members of the County Commissioners Court, other elected county officials and county employees ("Public Officials") may be called upon to answer questions from voters, the media, and other interested persons. Public Officials are required to walk a fine line in providing the public with necessary information while not, at the same time, running afoul of applicable statutory provisions.

This section of the Handbook provides an analysis of statutory provisions that prescribe the limits on and requirements of county officers and employees when providing information to the public about the election, or any measure set for an election.

1. Advertising

Statutory guidelines apply to the use of county funds in connection with providing information to voters about a measure that is set for election. State law prohibits an officer or employee of a political subdivision,[11] such as a county, from spending public funds for political advertising.[12] Included within this prohibition is an express ban on

[11] *See* TEX. ELEC. CODE ANN. § 1.005(13) (Vernon 2003) (defining "political subdivision").
[12] *See id.* at § 255.003(a).

knowingly using or authorizing the use of an internal mail system for the distribution of political advertising.[13] In the county's particular circumstance, care should also be exercised to ensure the county's websites or other governmental resources are not used in a manner that might subject the county to criticism that it is advocating for passage of the bond measure by inappropriate use of these resources. Texas Election Code Section 255.0031 prohibits a public officer or employee of a political subdivision from knowingly using the entity's internal mail system to distribute political advertising.

"Political advertising" includes communications that either support or oppose a measure.[14] The definition of political advertising encompasses communications that ***"in exchange for consideration"*** appear (1) on the radio, on television, in newspapers, magazines and other publications; (2) in pamphlets, circulars, fliers, billboards or other signs, bumper stickers, or similar forms of written communication; and (3) on an Internet website.[15] In more recent Texas Ethics Commission decisions, the consideration element does not appear to have been as important to the agency and they have sanctioned conduct even in situations where it is not clear that the placement of the ad or material was in exchange for consideration.

In addition, the county should review its policies for the use of county-owned facilities that may specify whether members of the community may have access to county facilities for the purpose of holding forums (either supporting or opposing the measures) or for filming political advertising that may ultimately be utilized by proponents or

[13] *See id.* at § 255.0031; *see also* OP. TEX. ETHICS COMM'N No. 45 (1992) (concluding that an officer or employee of a school district may not use or authorize the use of school personnel or equipment, including the school's internal mail system, for the distribution of political advertising).
[14] *See id.* at § 251.001(16).
[15] *See id.*

opponents of the measure. Familiarity with these rules will help ensure a fair and orderly communication with interested persons in the community who may inquire about such matters.

2. Neutral Information

The law allows political subdivisions to expend funds to publish information about the purpose of a measure as long as "the communication does not advocate passage or defeat of the measure."[16] The specific content of an advertisement will ultimately be the basis for a determination of a violation of the statutory provisions.[17]

Obviously, every effort should be made to assure that all communications from the county regarding facts or circumstances at issue in the bond election are made in a fashion that ensures their accuracy and does not advocate passage or defeat of the measure. More importantly, if it is necessary to issue county communications under such circumstances, it is best to avoid even the appearance of partiality.

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[16] *See id.* at § 255.003(b).
[17] *See* OP. TEX. ETHICS COMM'N NO. 102 (1992).

3. Interviews and Presentations

Oral presentations and interviews that occur at county functions or in county facilities (*e.g.*, commissioners court meetings, public hearings, etc.) in which public officials are required to make impromptu responses to inquiries about the bond election pose particularly difficult situations. Obviously, these types of oral presentations do not have the potential of causing a direct violation of Section 255.003 because there would not be a "publication" for consideration. However, we nonetheless recommend that public officials relay purely factual or objective information in these types of situations.

The use of a county facility or forum by public officials, to express subjective opinions or personal views about the election, can lead to the public perception that there is some misuse of public resources. Practically speaking, you can reasonably anticipate that public officials are all likely to field questions about the election while they are at work. While the county might consider appointing an information officer to whom complex questions about the election are routinely referred, all of the public officials will have to be able to respond to citizen inquiries. Keeping those comments limited to factual and objective information poses the least likelihood for problems. If appropriate, it may be useful for the speaker to mention during such an exchange that, as a public officer or employee, he/she is prohibited from utilizing county resources to advocate either passage or defeat of the measure.

Elected officials, officers and employees, while unable to utilize public resources for political advertising, are free to campaign for or against a measure on their <u>own time</u> and with <u>non-public resources</u>. County commissioners, the county judge and other elected county officials, as leaders in the community, can be particularly effective proponents of such measures for the county, and there is nothing that prohibits these officials, on their own time, from advocating for the bonds at civic meetings and in other forums in the community.

4. Enforcement

The Texas Ethics Commission ("Commission"), which is charged with administering Title 15 of the Texas Election Code, has interpreted the prohibition on the use of public funds for political advertising in a fairly strict manner. Violations of these statutes can result not only in complaints being filed with the Commission but also in criminal prosecution.[18] For example, in Texas Ethic Commission Decision SC-31509156 (2017), as the result of a sworn complaint being filed, the Commission fined the President of the Ysleta Independent School District for using school funds to publish a newsletter concerning the school district's bond issue. Citing to the Commission's brochure on the prohibition against using political subdivision resources for political advertising as well as other prior decisions of the Commission, the Commission found that the Trustee violated the law because statements in her "Greetings from the Board President" section of the newsletter were structured as a persuasive essay (stating a goal of quality education, identifying poor facilities as the problem preventing the goal and presenting the passage of the school bond measure as the solution to the problem). The Commission further found that including her personal preference for the measure to pass as well as a call to action, when viewed as a whole went beyond a mere factual description of the measure and advocated for its passage.[19]

City officials with the City of Haltom were fined due to the use of the term "attractive amenities" in a brochure regarding a bond election, and also for the use of a PowerPoint presentation with phrases such as "improve our parks and recreation areas" and "make

[18] A violation of Texas Election Code Section 255.003 is a Class A misdemeanor.
[19] *See* Texas Ethics Comm'n Order & Agreed Resolution in SC No. 13509156 (2017).

needed street improvements." The President of a Community College District was also fined due to a quote in a newsletter regarding a bond election, "we want to sustain the excellence" and "we are now asking voters if they too want to sustain the excellence." In both cases the individuals were fined because the Commission considered these to be "promotional statements" that exceeded a factual description of the purposes of a measure. [20]

So, it is clearly important that material in any brochures, websites, or other documents published at county expense describing the bond project remain as neutral and objective as possible and that officials avoid any subjective phrases that might be interpreted by the Commission in an adverse manner.

5. Political Committees

Political advertising and advocacy may, of course, be undertaken by private political committees so long as they properly register under Chapter 15 of the Election Code.[21] It is notable that in an election on a measure, as opposed to an election involving candidates for office, corporations and labor organizations may contribute to such a committee.[22]

6. Spanish-Speaking Voters

The law imposes not only limits but also requirements on communications made by the county to the public in relation to an election measure. State law generally requires that in election precincts in which five (5) percent or more of the inhabitants are of Spanish origin or descent, certain election materials be printed in English and Spanish.[23]

[20] *See e.g., In re Williams et al.,* SC-211170 (2004); *In re Israel,* SC-210964 (2002).
[21] *See e.g.,* TEX. ELEC. CODE ANN. § 251.001(13) (Vernon 2003).
[22] *See id*. at § 253.096.
[23] *See id.* at § 272.002.

In those same precincts, a county is to "make reasonable efforts to appoint a sufficient number of election clerks who are fluent in both English and Spanish."[24] Where the number of election clerks is insufficient to serve Spanish-speaking voters, a political subdivision must appoint at least one clerk who is fluent in both English and Spanish to serve at a central location to provide assistance to voters.[25] Additionally, federal law, specifically the Voting Rights Act, requires that whenever a political subdivision provides "materials or information relating to the electoral process . . . it shall provide them in the language of the applicable language minority group as well as in the English language."[26]

7. Summary

A county may not use public funds for advertising, mailings, etc., supporting or opposing the passage or defeat of a measure. It may use public funds to generate and disseminate accurate neutral information, but the dissemination of that information may not include advocacy of the passage or defeat of an electoral measure. The line between advocacy and dissemination of factual information may not always be clear, so care should be taken to ensure that any material from the county that might fall within the definition of advertising does not advocate a particular vote. Moreover, the county must ensure that its communications with the Hispanic population are effective by providing election materials and information in both Spanish and English, when applicable.

A bond election is a special election.

A bond election is a special election, even if it is held in conjunction with the General Election. Previously, the county was required to submit the election proceedings to the United States Department of Justice for review pursuant to the Voting Rights Act.

[24] *Id.* at § 272.009.
[25] *See id.*
[26] 42 U.S.C. 1973b(f)(4); *see also* 1973 aa-1a.

This changed with the decision by the United States Supreme Court on June 25, 2013 in *Shelby County, Alabama v. Holder*, 133 S.Ct. 2612 (2013), in which the Court held that it is unconstitutional to require states to obtain advance approval from the federal government before election laws can take effect. As such, preclearance from the Department of Justice for a bond election is no longer required.

C. Bond Election Timeline

Initially, the county must determine whether it can call a bond election for the particular purpose desired. For example, Chapter 1473, Texas Government Code, contains numerous provisions for issuing bonds for different types of buildings. Once the county confirms that the election may be called for the particular purpose, the county must determine when it can call the bond election.

1. Dates for Calling and Holding an Election

The following points apply to the determination of an election date and the calling of the election.

- An election may be held at a regular election date except for the May election date in even years.[27] This means that the election may be held on the first Saturday in May in any odd year, and on the first Tuesday after the first Monday in November of any year.

[27] The uniform election date in May of odd-numbered years if problematic for county special elections because the regular primary and potential primary run-offs span this same time period and would cause some confusion for voters and administrative challenges for the county.

- There is a 12-day window in which the county must call the election. It must call the election no earlier than 90 days before the election and no later than 78 days before the election. (Tex. Gov't Code §1251.003(c), Tex. Election Code § 3.005).
- Once the bond election has been approved, the county will not be able to sell bonds until 30 days from the canvass, so that the time has passed for an election contest.

2. Contents of the Election Order

Under any circumstance, the court must approve an order calling the bond election. The order will prescribe the measure to be voted, setting out the full proposition(s) and the actual ballot language. The requirements for the content of the order calling the bond election, as they relate to the bond, are prescribed in three provisions. Please note that Section 1251.052 was added to the Texas Government Code during the 2019 Legislative Session, and that Sections 57.072(e) and 3.009(b) of the Elections Code were amended by legislation enacted during that session as well:

I. Section 1251.052 of the Texas Government Code requires that the proposition to be voted on specifically state:

   (1) a plain language description of the single specific purposes for which the debt obligations are to be authorized;

   (2) the total principal amount of the debt obligations to be authorized; and

   (3) that taxes sufficient to pay the principal of and interest on the debt obligations will be imposed.

   This section also requires that "[e]ach single specific purpose for which debt obligations requiring voter approval are to be issued must be printed on the ballot as a separate proposition."

II. <u>Section 52.072 (e) of the Election Code</u> provides:

(e) In addition to any other requirement imposed by law for a proposition, including a provision prescribing the proposition language, a proposition submitted to the voters for approval of the imposition, increase, or reduction of a tax shall specifically state, as applicable:

(1) with respect to a proposition that only seeks voter approval of the imposition or increase of a tax, the amount of or maximum tax rate of the tax or increase for which approval is sought; or

(2) with respect to a proposition that only seeks voter approval of the reduction of a tax, the amount of the tax rate reduction or the tax rate for which approval is sought.

III. <u>Section 3.009(b) of the Texas Election Code</u> provides the following list of requirements that must be in the order calling an election for bonds or other voted obligations to be secured by ad valorem taxes:

(1) the proposition language that will appear on the ballot;

(2) the purpose for which the debt obligations are to be authorized;

(3) the principal amount of the debt obligations to be authorized;

(4) that taxes sufficient to pay the principal of and interest on the debt obligations may be imposed;

(5) a statement of the estimated tax rate if the debt obligations are authorized or of the maximum interest rate of the debt obligations or any series of the debt obligations, based on the market conditions at the time of the election order;

(6) the maximum maturity date of the debt obligations to be authorized or that the debt obligations may be issued to mature over a specified number of years not to exceed the maximum number of years authorized by law;

(7) the aggregate amount of the outstanding principal of the political subdivision's debt obligations as of the date the election is ordered, which may be based on the political subdivision’s expectations relative to variable rate debt obligations; and

(8) the aggregate amount of the outstanding interest on debt obligations of the political subdivision as of the beginning of the political subdivision's fiscal year in which the election is ordered; and

(9) the ad valorem debt service tax rate for the political subdivision at the time the election is ordered, expressed as an amount per $100 valuation of taxable property.

With the exception of item (5), counties were already required to comply with items (1) – (4) and (6) by Section 1251.002, Texas Government Code, and items (2) and (3) by Section 52.072(e) (1) of the Election Code. The financial advisor should be able to provide this information.

3. Publication of Notice of the Election

After calling the bond election, Section 1251.003(e) of the Government Code requires that the county must publish notice of the election in the county’s official newspaper on the same day of the week for two consecutive weeks. The first notice must be published no earlier than thirty days or later than fourteen days before the date of the election. This notice needs to include the full election order, not the short form that the Secretary of State has promulgated for other elections. It is in addition to the notice required by Section 4.003(c) of the Election Code. In addition to publication, Section 1251.003(d) requires that the notice must be posted on the bulletin board where the commissioners courts' open meetings notices are usually posted and three other public places in the county.

Section 4.003 (f) of the Election Code requires three additional posting requirements for bond elections:

> (f) A debt obligation election order required under Section 3.009 shall be posted:
>
> > (1) on election day and during early voting by personal appearance, in a prominent location at each polling place;
> >
> > (2) not later than the 21st day before the election, in three public places in the boundaries of the political subdivision holding the election; and
> >
> > (3) during the 21 days before the election, on the political subdivision's Internet website, prominently and together with the notice of the election and the contents of the proposition(s), if the political subdivision maintains an Internet website.

Item (2) is already required by Section 1251.003(d). However, items (1) and (3) will require posting that was not otherwise required. Item (1) will require posting of the order at each polling place. If the county has a website, the order must also be posted on the website.

Other statutes may have more specific requirements which also must be complied with. For instance, in order to call a bond election for a county hospital, Section 286.021, Texas Health and Safety Code, requires that the commissioners court receive a petition from voters requesting the election before it can be called and then the Court prescribes the measures to be voted on.

It is important for the county to have a detailed schedule of events that must occur in calling and conducting a bond election. The following timeline describes the major tasks the county will be required to complete to properly conduct a bond election:

Proposed Timeline for County Bond Election Process

90 days before
- First day to order election
- Texas Government Code §1251.003

78 days before
- Order calling Bond Election when called on a uniform election date must be 78 days before election
- Texas Election Code §3.005

77 days before / **21 days before**
- Post Notice and Order of Election at Courthouse, and Order of Election 3 Public Places in the county (Anytime after election has been called)
- Post Notice, Order, Sample Ballot and Proposition language on website
- Texas Government Code §1251.003(d)(1)(B)
- Must be posted by 21st day before
- Texas Election Code §4.003

30 days before / **14 days before**
- Publish First Notice of Election – Complete Order Calling Election (English and Spanish)
- Texas Government Code §1251.003(d)(2) & (e); Texas Election Code §4.003

- Publish Second Notice of Election – Complete Order Calling Election (English and Spanish) [same day of week in week following first publication]
- Texas Government Code §1251.003(d)(2) & (e); Texas Election Code §4.003

17 days before / **12 days before**
- First day of Early Voting (17th day before the November election and 12th day before the May election)
- Texas Election Code §85.001(a) & (e)
- Post order at each early voting location during early voting period
- Texas Election Code §4.003

4 days before
- Last day of Early Voting (4th day before election day)
- Texas Election Code §85.001(e)
- Post order at each early voting location during early voting period
- Texas Election Code §4.003

Election Day
- ELECTION DAY
- Post order at each polling place
- Texas Election Code §4.003

3 days after / **11 days after**
- *Canvass of May Election
- *Canvass of November Odd Year
- Texas Election Code §67.003

3 days after / **14 days after**
- *Canvass of November Even Year
- Texas Election Code §67.003

Later of 30 days after canvass or 30 days after election records are publicly available
- First day Bonds can be sold
- Election not final until after filing of contest period has expired
- Texas Election Code §233.006(b)

*First day of canvass may occur earlier if there are no provisional or overseas ballots.

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V. Securities Matters

Key Points

- *Typically a county will obligate itself to provide the market or the purchaser of its securities certain information for as long as the securities are outstanding.*
- *The Federal Securities and Exchange Commission is actively engaged in ensuring that municipal issuers, including counties, provide full disclosure about their past performance of disclosure obligations.*
- *This section of the handbook describes the fundamental disclosure obligations of a county and the role of the Securities and Exchange Commission in enforcing such obligations.*

A. Objectives of Federal and State Securities Laws

The marketing and sale of securities is regulated by the federal government under the Securities Act of 1933 (the "1933 Act") and the Securities Exchange Act of 1934 (the "1934 Act"), and by State law under the Texas Securities Act. Each of these sets of laws define the "securities" that they regulate in similarly broad terms that include bonds, certificates of obligations, notes, and any other evidence of indebtedness. (15 USCS §77b(a)(1) (1933 Act); 15 USCS § 78c (a) (10) (1934 Act); Ann. Texas Civ. St. Art 581-4(A) (Texas Securities Act)).

The objectives of the aforementioned securities laws overlap in significant ways in that each law serves to provide investors with meaningful information about the securities they purchase, and to prevent fraud and misrepresentation in the sale of securities.

The 1933 Act achieves these objectives by requiring the registration of non-exempt securities, by requiring the disclosure of financial and other information, and by expressly prohibiting the making of false or misleading statements, or the omission of material facts in connection with the sale of a security. The 1934 Act furthers the objectives by establishing the Securities and Exchange Commission (the "SEC") and giving it far-reaching authority over the securities market. The SEC's powers include the authority to require the registration of securities and oversight over securities brokers and dealers. The 1934 Act also prohibits the making of untrue statements of material facts, and the omission of material facts, in connection with the sale or purchase of a security. The Texas Securities Act established the State Securities Board, which is in many key ways analogous to the SEC. Like the 1933 Act and the 1934 Act, the Texas Securities Act requires the registration of securities and prohibits the use of fraud in the offer or sale of securities.

B. <u>Federal and State Securities Law as Applied to County-Issued Securities</u>

Securities that are issued by counties are exempt from many of the requirements imposed on non-exempt securities by the 1933 Act, the 1934 Act, and the Texas Securities Act. The requirements that do apply to county-issued securities, however, relate to the prohibitions against the use of false or misleading statements and against the misstatement or omission of **material** facts (the term "material" is defined in this section below) in the offer or sale of the securities, and obligations to provide continuing disclosure of certain information.

Before a county-issued security is sold by either a **competitive sale** or by a **negotiated sale**, the county's financing team will prepare an offering document, which typically is in the form of an "**official statement.**" The official statement is the document used to market the securities to potential investors and as such, it contains information about the project to be funded, the type and size of security being offered, the terms of repayment, and financial and demographic information about the county, as well as other material information that can be used to give potential purchasers of the securities a full picture of the investment.

As noted, the federal and State securities laws prohibit the use of fraud in the offer or sale of securities, including in the official statement. Moreover, the securities laws, as they apply to county-issued securities, prohibit the making of any untrue statement of, or misstatement of, a "**material"** fact, and the omission of any material fact that is required to make any statements made in regards to the offer or sale of the securities not misleading. For the purposes of the securities laws, information is "material," if there is a substantial likelihood that a reasonable investor would consider it important to an investment decision." (*In re* County of Orange, Cal., SEC Rel. Nos. 33-7260, 34-3676-(1996), citing *Basic v. Levinson*, 485 U.S. 224, 231-32 (1986); *TSC Industries, Inc. v. Northway, Inc.,* 426 U.S. 438, 449 (1976)).

Accordingly, the official statement must be drafted so as to include only true statements of material facts, and must include all of the material facts required to ensure that the official statement is not misleading.

Official statements, as well as any required continuing disclosure statements defined in the following section, are posted to the Electronic Municipal Market Access (EMMA) website, which is maintained by the Municipal Securities Rulemaking Board (MSRB), which in turn, is regulated by the SEC. Access to EMMA is free, and it is a good resource for anyone interested in studying official statements and continuing disclosure statements that have been submitted in connection with other sales of securities.

Although a county will only prepare an official statement when it sells its securities through a competitive or negotiated sale, the prohibitions against fraud, and the misstatement or omission or material information, apply to the county's sale of securities regardless of the type of sale. That is, these prohibitions will apply even the sale is through a private placement.

C. <u>Continuing Disclosure</u>

Rule 15c2-12 Obligations

A county that sells securities through a competitive sale or through a negotiated sale is required to provide the market annually updated financial information as well as notice of the occurrence of one or more specified events, which are listed below. Also, if a county sells its securities through a private placement, it will typically obligate itself to provide similar information. The county's obligations to provide such information will be referred to in this handbook as the county's "**continuing disclosure obligation**" or "**continuing disclosure undertaking.**"

A county's continuing disclosure undertaking is not directly imposed by the federal or state securities regulations. Rather, a county's obligations are derived from **SEC Rule 15c2-12 (the "Rule")**, which requires underwriters to obtain written assurances from the county that the county will perform the continuing disclosure obligations, before the underwriter participates in the purchase or sale of the securities. (Rule 15c2-12 is reprinted in Tab 4 to this handbook.)

Because of the overall importance of Rule 15c2-12 to the SEC's efforts to meet its objectives of ensuring that investors have access to meaningful information about the securities they purchase, and of preventing fraud and misrepresentation in the sale of securities, a portion of the Rule is copied, with minor editing for readability, below. Please note that the term "municipal securities" as used in the Rule includes securities issued by a county, and the term "obligated person" includes the county that issued the securities. Also, references to requirements to provide information to the Municipal Securities Rulemaking Board mean that the information must be provided to EMMA, which is discussed above. One relevant portion of the Rule is as follows:

The first paragraph of the Rule states the requirement that an underwriter obtain the written assurance of the issuer that the issuer will provide the information specified in the Rule in a timely manner. For county issuances, the county typically affirms its continuing disclosure undertaking in the order authorizing the issuance of securities. This paragraph also specifies that the information required to be provided under the rule will be provided to the market by posting on with EMMA.

Section 5(i)(C) of the Rule provides a list of events that the county must report to EMMA within ten days of occurrence. The occurrence of any of the specified events may indicate to the market weaknesses in the credit-worthiness of the security and as such, information about these events most likely would be "material" to any investment decisions about the underlying security. Moreover, the SEC requires the posting of notice of these events as a way of ensuring that investors have access to significant information about the security. It should be noted that items 15 and 16 are new additions to the list of reportable events and the requirement to report on these events became effective February 27, 2019.

Municipalities Continuing Disclosure Cooperation Initiative (MCDC)

The SEC has made it clear that it views any failure to provide notice of the events listed in Rule 15c2-12, including 5(i)(D), failure to provide annual financial information in a timely manner, as meaningful violations of the issuer's obligations, and that such violations carry substantial consequences.

In 2014, the SEC initiated the Municipalities Continuing Disclosure Cooperation Initiative ("MCDC"). The SEC, through MCDC, signaled that it would actively seek out violations of the Rule but, at the same time, encouraged issuers and underwriters to voluntarily admit violations to the SEC in exchange for lenient treatment (i.e., cease and desist letters, implementation of remedial steps, and no admittance of guilt).

As a result of MCDC, 71 issuers, which included some county issuers, had entered into settlements with the SEC for violations of reporting obligations. Many of the identified issuer violations related to the failure to timely file financial information and failure to provide notice that the issuer had missed a deadline for filing the financial information. In particular, the SEC found in many cases that if an issuer at any time in the previous five years had failed to make a timely filing of its financial information, e.g., filed the information 38 days late (as in one case), and did not disclose that it missed a deadline, the failure to provide such disclosure constituted the making of a false statement.

Although the SEC's enforcement actions taken through the MCDC initiative took place several years ago, the lessons learned are still fresh on the minds of many issuers. Moreover, the initiative has caused issuers to renew their focus on their continuing disclosure undertakings. Possibly one of the key takeaways is the importance SEC places on the accuracy and fullness of an issuer's description of its historical compliance with its disclosure obligations.

VI. Tax Matters

Key Points

- *The federal government views the tax-exempt status of securities as a subsidy to the counties.*

- *To maintain tax-exempt status of its securities, a county must observe tax regulations relating to the earning and use of* ***arbitrage*** *and the private use of the proceeds of the securities.*
- *This section of the handbook explains why tax-exempt status is viewed as a subsidy, describes in general terms the relevant tax laws, and discusses the consequences of non-compliance with those regulations.*

A. Tax-Exempt Status of Bonds is Considered a Subsidy to Counties

Most bonds issued by counties are issued on a tax-exempt basis; that is, interest income to the owner of the bond is excluded from federal income taxation. Section 103 of the Internal Revenue Code provides that for purposes of federal income taxation, gross income does not include interest on any state or local bond, that is, an obligation of a state or political subdivision thereof. Exceptions to this are **arbitrage bonds** and **private activity bonds**. If a county expects that the bonds will be private activity bonds or that the bonds will be arbitrage bonds (both terms are explained below), the county may consider issuing bonds on a taxable basis, i.e., bonds for which the interest income is taxable.

Federal tax law views the tax exemption as a subsidy to issuers because the exemption effectively lowers the issuer's borrowing costs by reducing the amount of tax that the federal government receives in connection with each tax-exempt bond. The amount by which the cost of borrowing is lowered is the amount of taxes that the federal government would be entitled to collect had the bonds been issued on a taxable basis. As noted above, the interest received by a holder of a tax-exempt bond is not subject to federal income tax. For that reason, investors can, within certain parameters, retain effectively higher rates of interest return with tax-exempt bonds than with taxable bonds, even though the taxable bonds have higher rates of interest. For example, if the bondholder pays a federal tax rate of 28%, then the bondholder will be able to keep $72 of every $100 of interest generated from the bond, whereas the bondholder is able to retain the full $100 of interest generated from a tax-exempt bond. This idea is illustrated in the table below which considers two bonds, one taxable and one tax-exempt, each in the principal amount of $100,000, and each with a different rate of interest.

Effect of Federal Income Tax on Investment
Taxable vs. Tax-Exempt

	5.00% Interest Rate Taxable	4.00% Interest Rate Tax-Exempt
Pre Tax Income	$ 5,000	$ 4,000
Federal Tax 28%	$ 1,400	0
After Tax Income	$ 3,600	$ 4,000

As shown above, the county is able to have a savings by borrowing money at a lower rate than the private sector and can still attract investors who can retain more of their investment income after taxes than they could at a higher taxable interest rate. The savings to the county is considered a subsidy by the federal government because that savings is the amount of taxes that the federal government forgoes by allowing the bonds to be tax-exempt.

There is an additional source of savings associated with tax-exempt bonds that are in the form of forgone tax revenue that relates to "**Bank Qualified Bonds**." Under Section 265(d) of the Internal Revenue Code, a county that expects to issue no more than $10 million of bonds in a calendar year can designate its bonds as "Bank Qualified" or "qualified tax-exempt obligations." This permits a financial institution which purchases the bonds to receive an 80% tax deduction for the interest cost on deposits used to purchase the bond issue. This makes the bonds more attractive to a financial institution. The interest rate on a Bank Qualified bond has historically been lower than a bond which is not Bank Qualified. The changes in federal tax law which became effective in 2018 may have reduced this impact and the county should consult with its financial advisor as to any potential benefits.

Because the federal government regards the tax-exempt designation as a federal subsidy, it has imposed very strict requirements relating to the issuance, investment of money prior to expenditure, uses of funds and other provisions that must be adhered to at the time the bonds are delivered and while the bonds are outstanding.

B. <u>Arbitrage and Rebate</u>

“Arbitrage,” for the purposes of the applicable federal tax rules, means the difference between the amount of interest earned on the investment of proceeds and the yield on the underlying bonds that is the source of the proceeds. For a general example, if a county issues bonds that have a yield of 3%, and then invests the proceeds of those bonds in an account that accumulates interest at a rate of 4%, the county would be earning arbitrate of 1%.

As a general matter, the county is allowed to earn that 1% of arbitrage for a limited period not to exceed three years, and that arbitrage must be ”rebated” to the federal government in payments made every five years. The period during which arbitrage may be earned can be less than three years depending on the type of bond and the purpose for which it is issued. A county may, in lieu of calculating the rebate amount, elect to pay a rebate in the form of a penalty equal to 1.5% of any unexpended proceeds. Before electing to pay this penalty, a county should consult with its bond counsel and financial advisor to determine if the election is financially beneficial for the county.

There are two exemptions from the rebate requirement. The first is the **"small issuer exemption"** which applies to an issuer who will not issue more than $5,000,000 of bonds in the calendar year in which the underlying bonds are issued. So-called "small issuers" are exempt from the rebate requirement. The other exemption is the "**spending exemption,**" which applies if the issuer spends down the proceeds within the prescribed time frame. To be eligible for the spending exemption, the issuer must spend the proceeds of the bond within either six months, 18 months, or 24 months, depending on the type of issuance.

C. <u>Private Activity Bonds</u>

One of the strongest rationales for the federal government's continued authorization of the use of tax-exempt status is that the bond proceeds are used to finance projects that benefit, and are of great importance to, the general public. Accordingly, there are rules that limit the extent to which a project funded with tax-exempt bonds can benefit a "private business." It should be noted that for the purposes of these restrictions, a "private business" includes non-profit entities as well as the federal government. If the bonds are used for a project that benefits a private business to a degree that is greater than what is allowed by the rules, the bonds will be deemed "private activity bonds," and will lose their tax-exempt status, unless the violation is cured in a timely manner. In determining whether a bond is a private activity bond, the federal government will apply what are known as the "private loan test" and the "private business tests." Under the private loan test, a bond is a private activity bond if more than a certain amount, which is the lesser of 5% of the bond proceeds or $5,000,000, is loaned to a non-governmental entity. Under private business tests, a bond is a private activity bond if more than 10% of the proceeds, or of the project financed with the proceeds, is used in the trade or business of anyone other than the county, and at the same time, at least 10% of the payment of the debt service on the bonds is secured by property used for a private business or is derived from payments related to property used for a private trade or business.

A private business use may arise if a nongovernmental entity or person has actual ownership of the property, actual or beneficial use of the property pursuant to a lease, or a management or incentive payment contract, or certain other arrangements such as a take or pay contract. If a tax-exempt bond financed project is sold or the use of the project is changed before the bonds are retired, remedial action may be necessary to ensure this change in the use of the project does not cause the bonds to become taxable. It is important to work with bond counsel before an action is taken that would cause bonds to become taxable so that remedial action can take place. It may be that bonds will have to be redeemed (and if not subject to current redemption, defeased) or that the proceeds are used for another governmental purpose.

D. <u>Exceptions</u>

The federal tax rules as they apply to tax-exempt bonds include numerous exceptions. Moreover, the preceding discussion of the arbitrage and rebate rules and the private activity bond rules should be read only as general summaries. Each of the requirements described above is subject to qualifications that may apply from situation to situation. The preceding discussions are presented for the purpose of giving the reader an idea of how the rules for tax-exempt bonds generally apply and are not intended to be the final word on any particular tax-related question.

The county's bond counsel, as a matter of course, will prepare a formal opinion as to the tax-exempt status of the bonds. In preparing its opinion, bond counsel will ascertain whether the county is in compliance with the federal tax requirements and that the county is able to take the actions required to maintain the tax-exempt status of the bonds.

E. The Federal Tax Certificate

The tax rules require that the issuer sign a federal tax certificate, often also known as an "no arbitrage certificate," that certifies the issuer's expectations with respect to the use of the bonds as of the date of issue. The certificate generally explains why the bonds comply with the applicable tax regulations and establishes the basis for designating the bonds as tax-exempt. This form typically is prepared by bond counsel.

F. Audit and Consequences of the Failure to Maintain Tax-Exempt Status

It is very important that the county keep reliable records of how the proceeds of its bonds, including any interest earned on those proceeds, are invested, managed, and spent. These records are necessary for the ongoing monitoring of compliance with the tax rules and also for the purpose of demonstrating compliance with the applicable tax rule in the event of an audit by the Internal Revenue Service. Any bond that is designated as tax-exempt is subject to audit by the IRS, which is very active in making sure that the aforementioned "subsidy" is not being abused by issuers.

Should the IRS determine that there is a problem in the way the county has treated its bond proceeds, the IRS could declare the interest on the bonds is taxable retroactive to the date of issuance. Generally, the IRS will pursue a policy of taxing bondholders only as a last resort and has expressed a preference to resolve tax-exempt bond infractions with other parties to the bond transactions, including the issuer. Consequently, the county will have the opportunity to remedy the problem and protect those who purchased its bonds. There are formal and informal settlement procedures available. The cost of bringing bonds back into compliance can be expensive and may involve redeeming outstanding bonds and payments to the IRS. This can prove to be a better solution than to allow the IRS to go after the bondholders, since this may subject the county to litigation from those that purchased the bonds because those purchasers have (1) lost the benefit of their tax-exempt income from their investment in the bonds, and (2) also incurred income tax liability for amounts that should have been paid but were not paid because the purchaser had relied on the county's representation that it would take no action that would cause the bonds to become taxable.

VII. SPECIAL TOPICS

A. Financing a County Jail

Planning and coordination are important in developing a construction project. Probably the most common construction project that most counties will have is the financing and construction of a new jail or expansion of an existing jail. The professionals most often used in a jail project are the financial advisor, bond counsel and architect, although other professionals are often involved. It is important that the county involve its financial advisor and bond counsel as early in the planning process as possible, even before an architect is retained. The bond counsel and the financial advisor can discuss which method of financing will be most efficient for the county based on the county's time frame and needs. They can provide practical insight on other jail projects and identify where problems have arisen. They can assist the county in its preparing for initial expenditures and have a reimbursement resolution ready when and if the county needs it. Unlike the architect, engineers and other professionals involved in the project, the county should have no out-of-pocket expense with bond counsel and financial advisor since they will be paid only if the bonds are issued.

After getting its financial advisor and bond counsel on board, the county should next hire an architect. It is important to have one who is experienced in designing a jail according to the requirements of the Texas Jail Standards Commission. Jail design is very different from designing a courthouse, an office building or a school. Remember, *the plans must be approved by the Jail Standards Commission*.

Architects tend to use an "AIA" contract, a preprinted contract designed by the American Institute of Architects. While the AIA contract forms are generally good, they tend to favor the Architect over the Owner (the county). As an example, the AIA Standard Form of Agreement between Owner and Architect (both the B-141 and the B-151 forms) permit the Owner to use the Architect's plans and specifications only for the particular construction project described in the contract and expressly prohibit the plans to be used "for future additions or alterations" to the project without the prior written consent of the Architect. The Standard AIA Form Agreement also waives consequential damages, which limits the Owner's ability to recover damages in the event of design errors and does not require the Architect to maintain professional liability insurance, which is the main coverage that insures against loss resulting from design errors. Consequently, if the county wants an architect agreement that has provisions different from these, the county should either use an AIA form that has been modified by the county's attorney to represent the interests of the county or it should use a different, more favorable, architect agreement form. In addition, the county should revise the document to provide that the architect will provide new drawings without additional cost to the county if the amounts bid on the contract exceed the architect's estimated construction cost. The modification to the AIA documents is done by either lining out certain provisions and adding replacement provisions in an attachment at the end of the AIA contract document or making the changes using the electronic version of the AIA document. The author prefers using a more county friendly manuscript contract, because the extensive number of changes to the AIA contract form needed to protect the county makes using the AIA document cumbersome. In any event, the resulting contract should be more "county friendly" so that the county and the architect are placed on a more equal relationship under the contract.

Because the architect will be billing the county from the moment he or she is hired, it is important to limit initial expenses and wait until after the financing has been approved before approving and authorizing additional expenses. The county should provide limitations in the contract for the amount that the architect will charge for this preliminary work in the event the county does not close on the financing. There are many reasons why the financing might not close. The most common would be that a bond election failed. Other reasons could be the inability to sell the bonds or a diminished need for the jail project, such as a reduction in the number of prisoners or finding another facility to house the prisoners in a less expensive manner than financing new jail bed construction.

To prepare for a jail financing, the county should first have the Jail Standards Commission provide the county with a needs analysis. Often architectural firms will offer to provide a needs study to suggest the proper size of the facility. However, the attorney general will not approve bonds or other financial obligations unless the Jail Standards Commission has approved the size as appropriate.

Once the Jail Standards Commission has provided a recommended size of the facility, the county should have the architect prepare initial plans that will be sufficient to provide a good estimate of the projected cost of the jail. As previously noted, there should be limits on how much the initial cost estimate will cost. It is also recommended that the contract documents provide that the architect is not authorized to proceed to the next phase and charge the county until financing has been approved.

Once the estimated cost of the jail facility is determined, the county will need to meet with its bond counsel and financial advisor to determine which method of finance will be most appropriate. Generally, jail projects are financed with a debt instrument that is backed by an ad valorem tax pledge. In some instances a revenue backed instrument might be appropriate.

A determination will be made by bond counsel on whether the county can use tax-exempt financing for the jail project. The type of prisoner that will be housed can adversely impact whether tax-exempt financing will be available. For facilities that house county prisoners or State prisoners, tax-exempt financing should be no problem. If the county is going to house federal prisoners, financing may have to be on a taxable basis unless the county contracts with the federal government using a short term contract that is for no longer than 100 days, although such a contract can be automatically renewable unless cancelled by one of the parties. Also, should the county decide to use a private operator to run the facility, it will have to use a management agreement that meets IRS requirements in order to use tax-exempt financing. The county will need to carefully review these issues with bond counsel before proceeding. The IRS has been auditing county facilities that were financed on a tax-exempt basis that primarily house federal prisoners.

Most county jail projects will use ad valorem tax backed debt instruments, such as general obligation bonds, certificates of obligation and in some instances tax notes. Tax-backed financing is the most efficient and least expensive method of finance for these projects. However, in some instances, a revenue backed obligation may be used, usually in the form of a Lease Purchase Agreement. Although lease purchase arrangements may provide a convenient, efficient form of financing, promoters of this method are often developers who come to the county with the financing already arranged. Because the developer has arranged the financing, it may not be the best deal for the county.

The county must analyze the reason for using the lease purchase financing. It is often represented that the revenues from the jail will pay for the project and that no tax levy will be required. While no debt tax levy is involved with a lease purchase financing, the county must first determine whether there will be adequate prisoners from other jurisdictions to cover the debt service. Most important is what will happen if the prisoners from other jurisdictions are removed. Will the county be able to afford the debt service? Will the county have a place to house its own prisoners? If a substantial number of prisoners from other jurisdictions are not available, the county will be paying for the jail through its maintenance and operations tax revenues, not a debt tax levy, so that a roll back situation may arise. A county considering a lease purchase arrangement should make an apples-to-apples comparison to determine the cost of the lease purchase arrangement to that of other forms of financing. The county's regular bond counsel and financial advisor should be asked to review the proposal because the county may not have adequate resources in-house to fairly evaluate the proposal and the risks involved.

B. Energy Savings Performance Contracts

One form of contract may not be recognized as a financing contract. Those contracts are Energy Performance Contracts under Chapter 302 of the Texas Local Government Code. Energy Savings Performance Contracts are defined in Section 302.001(4) as:

> "Energy savings performance contract" means a contract with a provider for energy or water conservation or usage measures in which the estimated energy savings, increase in billable revenues, or increase in meter accuracy resulting from the measures is subject to guarantee to offset the cost of the energy or water conservation or usage measures over a specified period. The term includes a contract for the installation or implementation of the following in new or existing facilities, including all causally connected work:

(A) insulation of a building structure and systems within the building;

(B) storm windows or doors, caulking or weather stripping, multiglazed windows or doors, heat-absorbing or heat-reflective glazed and coated window or door systems, or other window or door system modifications that reduce energy consumption;

(C) automatic energy control systems, including computer software and technical data licenses;

(D) heating, ventilating, or air-conditioning system modifications or replacements that reduce energy or water consumption;

(E) lighting fixtures that increase energy efficiency;

(F) energy recovery systems;

(G) electric systems improvements;

(H) water-conserving fixtures, appliances, and equipment or the substitution of non-water-using fixtures, appliances, and equipment;

(I) water-conserving landscape irrigation equipment;

(J) landscaping measures that reduce watering demands and capture and hold applied water and rainfall, including:

 (i) landscape contouring, including the use of berms, swales, and terraces; and

 (ii) the use of soil amendments that increase the water-holding capacity of the soil, including compost;

(K) rainwater harvesting equipment and equipment to make use of water collected as part of a storm-water system installed for water quality control;

(L) equipment for recycling or reuse of water originating on the premises or from other sources, including treated municipal effluent;

(M) equipment needed to capture water from nonconventional, alternate sources, including air-conditioning condensate or graywater, for nonpotable uses;

(N) metering or related equipment or systems that improve the accuracy of billable-revenue-generation systems; or

(O) other energy or water conservation-related improvements or equipment, including improvements or equipment relating to renewable energy or nonconventional water sources or water reuse."

These contracts should provide energy savings based on historical costs or avoided anticipated costs.

While energy savings is the focus, Chapter 302 includes a section on financing new air conditioning, heating, lighting and water equipment. Section 302.004(a) addresses financing:

Section 302.004. Method of Financing; Terms of Contract

(a) An energy savings performance contract may be financed:

(1) under a lease-purchase contract that has a term not to exceed

20 years from the final date of installation and that meets federal tax requirements for tax-free municipal leasing or long-term financing;

(2) with the proceeds of bonds; or

(3) under a contract with the provider of the energy or water conservation or usage measures that has a term not to exceed the lesser of 20 years from the final date of installation or the average useful life of the energy or water conservation or usage measures.

(a-1) Notwithstanding other law, the governing body of a local government may use any available money to pay the provider of the energy or water conservation measures under this section, and the governing body is not required to pay for such costs solely out of the savings realized by the local government under an energy savings performance contract. The governing body may contract with the provider to perform work that is related to, connected with, or otherwise ancillary to the measures identified in the scope of an energy savings performance contract.

(b) An energy savings performance contract shall contain provisions requiring the provider of the energy or water conservation or usage measures to provide a guarantee. If the term of the contract exceeds one year, the local government's contractual obligations in any one year during the term of the contract beginning after the final date of installation may not exceed the total energy and water savings, the net operating cost savings, and the stipulated or agreed upon increase in billable revenues resulting from the estimated increase in meter accuracy, divided by the number of years in the contract term.

Before approving a contract for energy performance savings, the county should have the prospective vendor provide the cost with and without financing. The reference to bonds in the statute is not limited to general obligation bonds. The attorney general has permitted the use of certificates of obligation for this purpose. Tax notes would also be permitted, but the county would be limited to a seven year financing rather than a 20 year financing.

The county should also require that the vendor provide a payment and performance bond. Section 302.003, Texas Local Government Code provides:

> **302.003. Payment and Performance Bond**
>
> Notwithstanding any other law, before entering into an energy savings performance contract, the governing body of the local government shall require the provider of the energy or water conservation or usage measures to file with the governing body a payment and performance bond relating to the installation of the measures in accordance with Chapter 2253, Government Code. The governing body may also require a separate bond to cover the value of the guarantee.

The terms of an energy performance savings contract should be reviewed by an attorney who is familiar with such contracts. If the county is going to use the lease purchase financing offered by the vendor, it should have the lease purchase portion reviewed by its bond counsel. Very often there are terms that are not in a county's best interest and usually can be negotiated to put the county in a more favorable position, as well as ensuring that the agreement complies with Texas law. It is also recommended that the county consult with its financial advisor to see if another financing option would be better for the county.

C. Public Finance for Economic Development

Economic development remains a very important consideration for Texas counties. The Texas Legislature provides new economic development tools in most legislative sessions. Counties have not been given the economic development tools that have been given to cities,[28] but some are available. While many of these tools do not involve the issuance of bonds, some do. For those that do, it may be a specially created entity rather than the county itself that issues the bonds. Counties can establish Economic Development Corporations under Chapter 501, Texas Local Government Code, and County Development Districts under Chapter 383 of the Local Government Code, and those districts can issue bonds. A Public Improvement District can be created under Chapter 372 of the Local Government Code to issue bonds.

1. Economic Development Corporations

Several counties have established Economic Development Corporations pursuant to the Development Corporation Act of 1979, Article 5190.6, Texas Civil Statutes. The county establishes an economic development corporation for economic development purposes. The economic development corporation is a non-profit corporation whose board is appointed by the commissioners court. The county must approve the articles of incorporation and bylaws, as well as any amendments.

[28] The legislature placed Proposition 4 on the November 8, 2011 ballot. This measure did not pass, but it would have given counties the authority to issue bonds to finance the development of unproductive, underdeveloped or blighted areas.

When a company decides to locate a facility in the county, it may be able to qualify for tax-exempt financing by going through the economic development corporation and the county. The economic development corporation serves as the conduit issuer for the company, and any bonds must be approved by the county.

For some companies, this financing is attractive. For others it is not. As a condition of getting the financing, the company must agree to comply with certain requirements in the Internal Revenue Code. In addition, the maximum amount that can be issued is $10,000,000.

In order to issue the bonds on a tax-exempt basis, an application must be filed with the State to obtain a portion of the private activity bond allocation. Once an allocation is obtained, the bonds must be issued and closed within a very short period of time.

The business entity must arrange its own financing. The county's bond counsel is usually involved in the financing, either as bond counsel for the economic development corporation or as counsel to the county and the development corporation, to protect the interests of the county and the development corporation. No county tax is pledged. The bonds are paid solely through the revenues of the facility being financed.

When a business entity approaches the county or economic development corporation to issue bonds on its behalf, it is important to analyze the economic basis of the proposal. The county's financial advisor can usually provide this service. The cost of the county's financial advisor and bond counsel can be included in the cost of the financing which is paid by the company requesting the financing.

The county and economic development corporation should develop a questionnaire which the company must complete that contains all of the information required to be filed with the State. In addition, the economic development corporation may establish a reasonable application fee to cover the cost of processing the matter through the State, as well as providing a nominal fee that is due upon closing. As a part of the application, an indemnification from the company requesting the financing can be required to protect the county, the economic development corporation and their officers and employees.

2. Public Improvement Districts

A county can create a Public Improvement District ("PID") under Chapter 372, Texas Local Government Code. A PID is an economic development tool that is available to both cities and counties. It provides a vehicle for a developer to obtain a source of funds for infrastructure in a project from assessments made upon property located within the project, so that the developer does not have to encumber his own funds for these purposes. PID revenues may only be used for infrastructure improvements that will benefit the public, such as streets, water and sewer lines.

In an unincorporated area, a developer would petition the county to create the PID. If the county agrees to create the PID, the county will then be asked to impose assessments on the property within the PID. Since all of the property is owned or controlled by the developer, there should be no controversy when the assessments are established. As the developer sells lots within the project, the purchasers (individuals and homebuilders) will become responsible for the payment of the assessments.

Often developers will want a county to enter into a development agreement in which the county would agree to create the PID and to execute a promissory note, payable only from PID revenues, and approve bonds for the project based solely on PID revenues.

Counties should review these proposals carefully. If a county decides to pursue a project, it should consider eliminating any promissory note obligation for the county and require that the developer or ultimately the PID would pay for any expense incurred by the county. A county should also consider creating a Public Facility Corporation to administer the PID and require that the name of the PID not contain a reference to the county.

In order to create a PID, a petition is submitted to the county signed by the owners of more than 50% of the taxable real property of the area to encompass the proposed PID, and record owners of real property liable for assessment under the proposal who (A) constitute more than 50% of all record owners with property that will be liable for assessment, or (B) own taxable real property that constitutes more than 50% of the area of all taxable real property that will be liable for assessment. Here, the developer will own all of the property that will be proposed to encompass the PID. Ideally, the county would adopt a PID policy that covers the county's requirements and require that any petition for the creation of a PID conform to that policy. By adopting a PID policy, the county can ensure that its most pressing concerns have been resolved in advance.

Once the petition is received, the county is required to hold a public hearing. Before holding the hearing, the county can require preliminary estimates and evaluations of the proposal and a feasibility study. If the county goes with the PID, the county will want the developer to provide sufficient information to permit an informed decision, including assurance that the PID will generate sufficient revenues to cover debt service. Once the county is satisfied with the information, it convenes a hearing. There are specific notice requirements that must be met in order to hold the hearing. Once these are satisfied, the county would conduct a hearing. Within six months from the date of the hearing, the commissioners court may create the PID.

After the PID has been created, the developer through its consultant will work up the proposed assessment and service plan. Once this is in final form, the plan is presented to the commissioners court for adoption. A public hearing is then set on the plan. At or upon adjournment of the hearing, the county will hear any objections to the proposed assessments. The commissioners court will then determine the assessments to impose and pass an order to that effect. The developer would have the county issue bonds based on the revenues generated by the assessments.

The problem is that once the plan has been accepted, the county's role is not over. It will need to provide for the calculation of the assessments and will have ongoing responsibility to approve a new service plan annually. Both of these functions typically are performed by a third-party known as the "PID Administrator." Payment for the services of the PID administrator is made from the bond proceeds and the collected assessments.

The County will be the focal point for complaints about the assessments which can generate political problems for the incumbent officeholders. The county will also be required to pursue property owners who fail to pay their assessments. This can create political problems, especially if the county is required to foreclose on the property. The county will probably want to negotiate with the law firm that collects the county's delinquent taxes to also pursue property owners who are not timely in paying their assessments.

The general concept of creating a PID is fairly straightforward. However, the details must be carefully considered. The commissioners court will want to make certain that the county is adequately protected in any document presented for the county to approve.

3. County Development Districts

Chapter 383, Texas Local Government Code, authorizes a county with a population of 400,000 or less to create a county development district. To do so, it must first receive a petition which is accompanied by a consent from all holders of fee simple title in the proposed district. A hearing is held on the petition, and if the county approves, it will call an election on the creation of the district and the adoption of a sales and use tax for the development of tourism. If passed, the district, rather than the county, issues bonds secured by the pledge of the sales and use tax or other revenues.

TAB 1 – KEY TERMS

Arbitrage – For the purposes of federal tax law as it applies to tax-exempt securities issue by a county, arbitrage is the difference between the amount of interest paid on the security and amounts earned by investing the proceeds of the security. Federal tax law restricts the periods during which a county may earn arbitrage as well as the usage of any arbitrage earned.

Arbitrage Bonds – Bonds issued as tax-exempt that are deemed by the IRS to be in violation of the tax-regulations relating to arbitrage.

Bank Qualified Bonds – Bonds issued by a county that expects to issue no more than $10 million of bonds in a calendar year that are designated by the county as "Bank Qualified" or "qualified tax-exempt obligations." The designation permits a financial institution which purchases the bonds to receive an 80% tax deduction for the interest cost on deposits used to purchase the bond issue.

Certificates of Obligation – Securities issued under Subchapter C of Chapter 271 of the Texas Local Government Code. See Table 2 for a description of key aspects of certificates of obligation, as a form of debt obligation.

Competitive Sale – A method of sale in which the issuer, through a notice of sale, asks underwriters to submit firm offers to purchase the county's securities. Offers must comply with the terms of the notice of sale.

Continuing Disclosure Agreement – An agreement where the issuer, or other person or entity, obligates itself to provide certain financial and operating information on an ongoing basis. The information required to be provided typically includes the information required to be disclosed under **Rule 15c2-12.**

Debt – Any financial obligation of a county that cannot be paid out of currently available funds or the current annual budget. State law prohibits a county from issuing debt unless there is express constitutional or statutory authority to do so.

Disclosure Obligations/Undertakings – The County's obligations to provide annual financial information, specified operating information, and notice of the occurrence of certain events as required under **Rule 15c2-12**. A county typically confirms its obligation to provide the required information in the order authorizing the sale of the securities.

Federal Tax Certificate – The federal tax regulations that apply to tax-exempt bonds require the issuer to certify its expectations as to the use and management of the security proceeds. The federal tax certificate, also known as the **no arbitrage certificate,** is the form that this certification takes.

General Obligation Bonds – Bonds secured by the county's ad valorem taxing power. The bonds are issued after approval at a bond election.

Material – In the context of securities law, information is material, and should be disclosed in any documents used to market the securities, if there is a substantial likelihood that a reasonable investor would consider it important to an investment decision. Whether information is material will vary from transaction to transaction.

Negotiated Sale – A method of selling the county's securities whereby the securities are sold directly to an underwriter selected by the county without a competitive process.

P-Letter – The Preliminary Approval Letter issued by the attorney general after its initial review of the **transcript**. The P-Letter specifies what additional information or materials the attorney general will need to approve the securities.

Private Activity Bonds – Bonds of which the proceeds are used by one or more private entities, or the federal government, in amounts that exceed the thresholds established by the applicable federal tax regulations. Private activity bonds are not eligible for tax-exempt status unless they are used for qualified purposes that are expressly stated in the tax regulations.

Private Placement – A method of selling the county's securities whereby the securities are sold directly to an investor or entity. The purchaser typically will be subject to restrictions as to the resale of the securities.

Public Securities – Contractual debt obligations of the county.

Rebate – The amount required to be paid by the county to the federal government based on the county's **arbitrage** earnings.

Reimbursement resolution – Resolution declaring county's intent to reimburse itself from the proceeds of a debt obligation for expenses incurred and paid before the proceeds are received. Federal tax law typically requires a reimbursement resolution for certain categories of expenditures.

Rule 15c2-12 – The federal securities regulation that requires underwriters to obtain written assurances from the county that the county will provide certain annual financial information as well as notice of the occurrence of specified events for so long as the subject securities are outstanding.

Small Issuer Exemption – An exemption from the requirement that a county pay **rebate** to the federal government that applies if the county reasonably expects to issue no more than $5,000,000 in securities during the calendar year.

Spending Exemption – An exemption from the requirement that a county pay **rebate** to the federal government that applies if the county spends the proceeds of the securities within certain timeframes that vary depending on the purpose of the proceeds.

Transcript – The collection of agreements and official actions that together make up the bond transaction.

TAB 2 – TEXAS ATTORNEY GENERAL OPINION JC-0139

November 3, 1999

The Honorable James W. Carr
Lavaca County Attorney
P.O. Box 576
Hallettsville, Texas 77964-0576

Opinion No. JC-0139

Re: Whether a county may borrow money from the State Infrastructure Bank for road and bridge construction and repay the loan with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan (RQ-0057-JC)

Dear Mr. Carr:

You ask whether Lavaca County may borrow money from the State Infrastructure Bank ("the Bank") for road and bridge construction and repay the loan with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan. County authority to enter into debt must be express or necessarily implied by statute. Because no statute expressly or impliedly authorizes a county to borrow money from the State Infrastructure Bank in the manner proposed here, the county may not borrow funds from the Bank and repay the loan with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan.

The State Infrastructure Bank is governed by chapter 222, subchapter D of the Transportation Code, which the legislature enacted in 1997.[1] The legislature created the Bank within the Department of Transportation to take advantage of a new federal program to fund highway construction,[2] and subchapter D mirrors the federal law providing for state infrastructure banks, *see* National Highway System Designation Act of 1995, Pub. L. No. 104-59, § 350, 109 Stat. 568, 618; *see also* Transportation Infrastructure Finance and Innovation Act of 1998, Pub. L. No. 105-178, § 1511, 112 Stat. 251. Pursuant to subchapter D, the purpose of the Bank is to "encourage public and private investment in transportation facilities" and to "develop financing techniques designed to [] expand the availability of funding for transportation projects and to reduce direct state costs;

[1]Act of June 1, 1997, 75th Leg., R.S., ch. 1711, § 1.21, secs. 222.071-.078, 1997 Tex. Gen. Laws 4427, 4433-36.

[2]*See* SEN. COMM. ON INTERNATIONAL RELATIONS, TRADE AND TECHNOLOGY, BILL ANALYSIS, Tex. S.B. 370, 75th Leg., R.S. (1997); SEN. COMM. ON INTERNATIONAL RELATIONS, TRADE AND TECHNOLOGY, BILL ANALYSIS, Tex. Comm. Substitute S.B. 370, 75th Leg., R.S. (1997).

[] maximize private and local participation in financing projects; and [] improve the efficiency of the state transportation system." TEX. TRANSP. CODE ANN. § 222.073 (Vernon 1999). To further these purposes, the Transportation Commission may use money in the Bank "to provide financial assistance to a public or private entity for a qualified project." *Id.* § 222.074(a). It may do so by extending credit by direct loan, providing credit enhancements, serving as a capital reserve for bond or debt instrument financing, subsidizing interest rates, insuring the issuance of a letter of credit or credit instrument, financing a purchase or lease agreement in connection with a transit project, providing security for bonds or other debt instruments, or providing methods of leveraging money that have been approved by the United States Secretary of Transportation and relate to the project for which the assistance is provided. *See id.* § 222.074(a)(1)-(8). The Transportation Commission has adopted rules specifying the procedures and conditions for applying for and obtaining assistance from the Bank. *See* 43 TEX. ADMIN. CODE ch. 6 (1999).

Lavaca County would like to borrow money from the State Infrastructure Bank and forego the expense of issuing bonds or certificates of obligation under chapter 271 of the Local Government Code or anticipation notes under chapter 1431 of the Government Code, formerly article 717w of the Revised Civil Statutes,[3] to evidence its agreement to repay the money it has borrowed. *See* Letter from Honorable James W. Carr, Lavaca County Attorney, to Elizabeth Robinson, Office of the Texas Attorney General (Apr. 5, 1999) (on file with Opinion Committee). Rather, the county would merely commit future tax revenue to repay the loan. *See id.* Presumably, the county would evidence the borrowing by entering into an agreement with the Bank. The county would levy a sufficient tax to pay the principal and interest on the debt as required by section 7 of article XI, which mandates cities and counties, at the time a debt is created, "to levy[] and collect[] a tax sufficient to pay the interest thereon and [to] provide . . . a sinking fund," TEX. CONST. art. XI, § 7. *See* Brief from Honorable James W. Carr, Lavaca County Attorney, to Elizabeth Robinson, Office of the Texas Attorney General (Apr. 14, 1999) (on file with Opinion Committee). The total tax levy would not exceed the constitutional limitation on the county tax rate set forth in section 9 of article VIII. *See id.*

Commissioners courts do not have a general power to incur debt, which, in this context, is generally defined as "any pecuniary obligation imposed by contract, except such as will, at the date of the contract, within the lawful and reasonable contemplation of the parties, be satisfied out of current revenues for the year, or out of some fund then within the immediate control of the city [or county]." *City of Bonham v. Southwest Sanitation, Inc.*, 871 S.W.2d 765, 768 (Tex. App.–Texarkana 1994, writ denied) (defining "debt" for purposes of article XI, section 7 of the Texas Constitution, which provides that a city or county is prohibited from creating a debt unless at the same time it

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[3]The 76th Texas Legislature repealed former articles 701-705, 717q, 717w, and 726 of the Revised Civil Statutes and codified them without substantive change in Title 9 of the Government Code, the Public Securities Title. *See* Act of May 10, 1999, 76th Leg., R.S., ch. 227, § 1, secs. 1251.001-.005, 1371.001-.106, 1431.001-.013, 1471.001-.087, 1999 Tex. Sess. Law Serv. 721, 775, 786, 817, 834; *id.* § 28, 1999 Tex. Sess. Law Serv. at 1056 (repealing articles 701-705, 717q, 717w, and 726). For ease of citation, this opinion will refer to the provisions of Title 9 as they will be codified in the Government Code.

provides for payment of the debt). As one commentator has stated, "Counties have no statutory authority to merely borrow money from a bank." 35 DAVID B. BROOKS, TEXAS PRACTICE: COUNTY AND SPECIAL DISTRICT LAW § 17.27 (1989); *see also* Tex. Att'y Gen. Op. No. JM-274 (1984) at 1 ("Counties lack authority to borrow money except through the issuance of bonds, certificates of obligation, or other forms of indebtedness which are specifically authorized by law."). Courts have long held that the authority of a commissioners court to make contracts on behalf of the county is limited to that conferred either expressly or by necessary implication by the constitution and laws of the state. *See, e.g., Childress County v. State*, 92 S.W.2d 1011, 1016 (Tex. 1936); *Jack v. State*, 694 S.W.2d 391, 397 (Tex. App.–San Antonio 1985, writ ref'd n.r.e.). In the area of public finance, courts have been particularly reluctant to imply the authority of a local government, such as a county, to enter into debt. *See, e.g., San Antonio Union Junior College Dist. v. Daniel*, 206 S.W.2d 995, 999 (Tex. 1947) (and cases cited therein) (power to issue negotiable paper for improvements beyond powers of city or county unless specially granted; when granted, may only be exercised in mode and for purposes specified); *Lopez v. Ramirez*, 558 S.W.2d 954, 957 (Tex. Civ. App.–San Antonio 1977, no writ) (statutes regarding authority to create debt must be strictly and narrowly construed) (citing *Robertson v. Breedlove*, 61 Tex. 316 (1884), and *Daniel*, 206 S.W.2d 995); *see also* Tex. Atty. Gen. Op. No. JC-0036 (1999) at 10 ("Provisions authorizing a local government to create debt must be strictly and narrowly construed.") (citations omitted).

A number of provisions expressly authorize counties to levy taxes to pay for road and bridge construction, *see* TEX. CONST. art. III, § 52(b), (c) (authorizing unlimited taxes to secure road bonds); *id.* art. VIII, § 9 (authorizing county to levy taxes including taxes for road and bridge construction and maintenance); *see also* TEX. TRANSP. CODE ANN. §§ 256.001 (Vernon 1999) (authorizing use of county road and bridge fund); 256.051 (authorizing levy of bond taxes), and to finance road and bridge construction by issuing bonds and other debt instruments secured by a pledge of those taxes, *see, e.g.*, TEX. GOV'T CODE ANN. §§ 1251.001-.005, 1431.001-.013, 1471.001-.087;[4] TEX. LOC. GOV'T CODE ANN. ch. 271 (Vernon 1999). No provision authorizes a county to simply borrow money from a bank to pay for road and bridge construction and to pledge future ad valorem property taxes to repay the loan.

Generally, statutes that authorize a county to borrow funds for road and bridge construction require the issuance and sale of bonds or other obligations in compliance with statutory procedures, including approval by the Attorney General. *See, e.g.*, TEX. GOV'T CODE ANN. § 1431.004(a)(1)(A) (authorizing anticipation notes to pay for a contractual obligation incurred or to be incurred for the construction of a public work); *id.* ch. 1471 (providing for county and road district road bonds);[5] TEX. LOC. GOV'T CODE ANN. ch. 271 (Vernon 1999) (authorizing certificates of obligation to pay for contractual obligation to be incurred for the construction of any public work). These obligations are sold to purchasers in exchange for money, which is used for county projects. The obligations evidence a loan made by the purchaser to the county and the county's agreement to repay the money

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[4]*See supra* note 3.

[5]*See supra* note 3.

it has borrowed. *See* BLACK'S LAW DICTIONARY 178 (6th ed. 1990) (a "bond" is "evidence of a debt on which the issuing . . . governmental body promises to pay the bondholders a specified amount of interest for a specified length of time, and to repay the loan on the expiration date"); 22 ISAAC SINGER, TEXAS PRACTICE: MUNICIPAL LAW AND PRACTICE § 303 (1976) (a "bond is evidence of creation of a debt"). In addition, in *Lasater v. Lopez*, 217 S.W. 373 (Tex. 1919), the Texas Supreme Court recognized the authority of counties to pay road construction contractors for work performed with interest-bearing warrants payable in future years as a necessary authority that preexisted counties' power to issue bonds for road and bridge construction.

The county's query suggests that the county is authorized to borrow the funds and to pledge taxes to repay the debt without issuing bonds or other obligations provided that the county complies with the strictures of section 7 of article XI. However, this provision imposes conditions on the creation of debt; it does not authorize creation of debt. *See* Tex. Att'y Gen. Op. No. DM-467 (1998) at 7 n.18 ("Article XI, section 7 [of the Texas Constitution] limits the authority of a county to incur debt; it does not affirmatively authorize counties to levy taxes for any purpose. . . . Therefore, before providing for a levy and sinking fund in order to comply with article XI, section 7, a county should first verify that it is authorized to levy the tax.") (citing *Mitchell County v. City Nat'l Bank*, 43 S.W. 880, 883 (Tex. 1898) (Texas Constitution article XI, section 7 "contains no grant of authority to levy a tax")). Compliance with section 7 of article XI by providing to repay borrowed funds is not a sufficient basis for a county to borrow the funds. If that were the case, there would be no need for the many statutes authorizing the issuance of bonds and other obligations. For the same reason, the mere fact that the loan may be repaid without exceeding the article VIII, section 9 ceiling for the county tax rate is not a sufficient basis for a county to borrow the funds.

A brief submitted by the Department of Transportation suggests that the authority of a county to borrow money from the State Infrastructure Bank and pledge tax revenues to repay the loan without issuing bonds or other obligations may be inferred from the provisions in the Transportation Code creating the Bank, particularly section 222.074 of subchapter D, which authorizes the Bank to "extend credit by direct loan," TEX. TRANSP. CODE ANN § 222.074 (Vernon 1999). *See* Letter Brief from Richard D. Monroe, General Counsel, Department of Transportation, to Elizabeth Robinson, Office of the Texas Attorney General, at 2 (July 29, 1999) (on file with Opinion Committee) [hereinafter "DOT Brief"]. For the reasons explained below, we disagree.

No provision in subchapter D expressly authorizes a county to borrow funds from the State Infrastructure Bank. Nor do we believe that county authority to borrow funds from the Bank must be necessarily implied by subchapter D. The Bank is authorized to assist both public and private entities in a variety of ways: It may assist directly by making a loan or, more indirectly, by generally enhancing, insuring, or subsidizing payments securing debt issued by these entities to finance a project. *See* TEX. TRANSP. CODE ANN. § 222.074 (a)(1)-(8) (Vernon 1999); *see also* National Highway System Designation Act of 1995, Pub. L. No. 104-59, § 350(c), (*l*)(3), 109 Stat. 568, 618; Transportation Infrastructure Finance and Innovation Act of 1998, Pub. L. No. 105-178, § 1511(a)(1), (d), 112 Stat. 251 (defining "other assistance" to include providing credit enhancements, serving as capital reserve for bonds or debt instruments, subsidizing interest rates, ensuring issuance of letter of credit and credit instruments, financing purchase and lease agreements, providing debt security, and providing other debt financing and leveraging approved by the United States Secretary of Transportation; and providing that a state infrastructure bank "may make loans or provide other assistance to a public or private entity in an amount equal to all or part of the cost of carrying out a project eligible for assistance").

Counties need not borrow funds from the State Infrastructure Bank in the manner proposed by the county in order to participate in the Bank's assistance programs. Counties may be able to participate in the types of assistance the Bank is authorized to provide, within the statutory framework for county financing, in several ways. With respect to the direct loan assistance, for example, a county may issue bonds or other obligations that it is expressly authorized to issue for road and bridge construction and sell them to the Bank in exchange for the "loan" of the funds or purchase price. Neither subchapter D nor the Transportation Commission rules limit how a "direct loan" is to be evidenced or made and, in fact, subchapter D appears to contemplate that the Bank will acquire "obligations" that evidence loans it has made. *See* TEX. TRANSP. CODE ANN. § 222.075(d) (Vernon 1999) (revenue bonds issued to obtain funds for Bank payable in part from principal and interest payments paid on "acquired obligations"), (f) (Transportation Commission may require participants to make charges, levy taxes, or otherwise provide for sufficient money to pay "acquired obligations").

In addition, counties may be able to participate in the more indirect assistance the Bank is authorized to provide. For example, the Bank may provide credit enhancement to a county authorized to execute credit agreements for obligations issued to finance transit projects. *See id.* § 222.074(a)(2); TEX. GOV'T CODE ANN. § 1371.001(1), (4), .056 (authorizing certain issuers, including home-rule cities and counties with certain population, to enter into credit agreements in connection with issuance of bonds or other obligations).[6] Furthermore, subchapter D appears to authorize the Bank to "subsidize" interest payments on county obligations or to serve as a reserve fund on such obligations, presumably enhancing the obligations' security and marketability.

Neither the county nor the Department of Transportation asserts that the county cannot obtain a loan from the Bank using traditional statutory financing methods. Rather, the county indicates that it would like to obtain a loan from the Bank without following statutorily required procedures. But these procedures are not optional; issuing bonds or other obligations is the exercise of the issuer's borrowing authority in accordance with legislatively mandated procedures.

Given that the Bank may assist a variety of entities in a variety of ways, that it is not limited to loaning funds only in the manner proposed by the county (*i.e.*, without the county issuing bonds and or other obligations), and that counties are authorized to participate in some forms of assistance that the Bank has been established to provide, the authority of a county to borrow bank funds is not essential to the Bank achieving its statutory purpose. Therefore, the authority of a county to borrow money from the Bank may not be necessarily implied by subchapter D.

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[6] *See supra* note 3.

The brief from the Department of Transportation also observes that state law authorizes counties to construct and maintain roads and bridges and to levy taxes for those purposes. *See* DOT Brief at 2 (citing TEX. TRANSP. CODE ANN. §§ 251.081 (Vernon 1999) (authorizing commissioners court to erect and maintain any necessary bridge in the county); 256.001 (county road and bridge fund)); *see also* TEX. TRANSP. CODE ANN. § 251.003 (Vernon 1999) (authorizing commissioners court to construct and maintain public roads). The brief states that the "power to create debt [to build and improve county roads and bridges] is implicit in the grant of authority to levy taxes to build and improve county roads and bridges," citing *Lasater v. Lopez* and Attorney General Opinion JM-642. DOT Brief at 2. But neither opinion stands for the proposition that county authority to borrow money must be implied by these statutes.

In *Lasater v. Lopez*, the court did not conclude that the authority to borrow money may be implied. Rather the court held that the county could pay for road construction by issuing interest-bearing county warrants. As subsequent courts have noted, there is a difference between obtaining property or labor on credit, which *Lasater* sanctioned, and borrowing money, which *Lasater* did not address. "Borrowed money can be diverted from its legitimate purpose and the voters deprived of any benefit therefrom, but there is no such danger when authorized services or improvements are obtained by the public on credit." *San Antonio River Auth. v. Shepperd*, 299 S.W.2d 920, 925 (Tex. 1957) (citing *Bridgers v. City of Lampasas*, 249 S.W. 1083, 1085 (Tex. Civ. App.–Austin 1923, writ ref'd)); *see also Adams v. McGill*, 146 S.W.2d 332, 335 (Tex. Civ. App.–El Paso 1940, writ ref'd); Tex. Att'y Gen. Op. No. JM-697 (1987) at 5-6 (noting that *Shepperd* relied on the distinction between obtaining authorized services or improvements on credit and borrowing money; equating purchase of jail by lease-purchase contract with the former rather than the latter). Thus, *Lasater* implies from statutes authorizing counties to expend money to make improvements the authority to obtain property and labor on credit; it does not imply authority to borrow money.

Nor does Attorney General Opinion JM-642 provide support for the proposition that a county has implied authority to borrow money for bridge and road construction. That opinion concluded that a joint city-county hospital board is authorized to borrow funds to purchase equipment and make renovations based on the entity's express authority to establish and equip a hospital. Its conclusion is expressly limited to a joint city-county hospital created under former article 4494i of the Revised Civil Statutes. *See* Tex. Att'y Gen. Op. No. JM-642 (1987) at 8-9. And, in an opinion on a county's implied authority to use its credit to purchase or construct a jail issued just a few months after Attorney General Opinion JM-642, this office concluded that the prior opinion was inapplicable because it "relied on the power of the home rule city in question to borrow funds." Tex. Att'y Gen. Op. No. JM-697 (1987) at 2. Thus, to the extent Attorney General Opinion JM-642 suggests that a county may have implied authority to borrow money, it has not been followed. We are not aware of any other attorney general opinion concluding that a county has implied authority to borrow funds.

In sum, county authority to enter into debt must be express or necessarily implied by statute. Subchapter D of chapter 222 of the Transportation Code neither expressly nor by implication authorizes a county to borrow funds for road and bridge construction from the State Infrastructure

Bank and to repay the Bank with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan. Neither *Lasater v. Lopez* nor Attorney General Opinion JM-642 supports the conclusion that a county has implied authority to borrow funds for road and bridge construction. Because no statute expressly or impliedly authorizes a county to borrow money from the State Infrastructure Bank in the manner proposed here, we conclude that Lavaca County may not borrow funds from the Bank and repay the loan with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan. Of course, counties may borrow money from the Bank using traditional statutory financing methods for road and bridge construction.

SUMMARY

A county may not borrow money from the State Infrastructure Bank for road and bridge construction and repay the loan with the proceeds of ad valorem property taxes levied for that purpose over a term of years without issuing bonds or other obligations evidencing the loan.

Yours very truly,

John Cornyn

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TAB 3 – CONSTITUTIONAL PROVISIONS ON COUNTY DEBT

Article III, Sec. 52. RESTRICTIONS ON LENDING CREDIT OR MAKING GRANTS BY POLITICAL CORPORATIONS OR POLITICAL SUBDIVISIONS; AUTHORIZED BONDS; INVESTMENT OF FUNDS.

(a) Except as otherwise provided by this section, the Legislature shall have no power to authorize any county, city, town or other political corporation or subdivision of the State to lend its credit or to grant public money or thing of value in aid of, or to any individual, association or corporation whatsoever, or to become a stockholder in such corporation, association or company. However, this section does not prohibit the use of public funds or credit for the payment of premiums on nonassessable property and casualty, life, health, or accident insurance policies and annuity contracts issued by a mutual insurance company authorized to do business in this State.

(b) Under Legislative provision, any county, political subdivision of a county, number of adjoining counties, political subdivision of the State, or defined district now or hereafter to be described and defined within the State of Texas, and which may or may not include, towns, villages or municipal corporations, upon a vote of two-thirds majority of the voting qualified voters of such district or territory to be affected thereby, may issue bonds or otherwise lend its credit in any amount not to exceed one-fourth of the assessed valuation of the real property of such district or territory, except that the total bonded indebtedness of any city or town shall never exceed the limits imposed by other provisions of this Constitution, and levy and collect taxes to pay the interest thereon and provide a sinking fund for the redemption thereof, as the Legislature may authorize, and in such manner as it may authorize the same, for the following purposes to wit:

(1) The improvement of rivers, creeks, and streams to prevent overflows, and to permit of navigation thereof, or irrigation thereof, or in aid of such purposes.

(2) The construction and maintenance of pools, lakes, reservoirs, dams, canals and waterways for the purposes of irrigation, drainage or navigation, or in aid thereof.

(3) The construction, maintenance and operation of macadamized, graveled or paved roads and turnpikes, or in aid thereof.

(c) Notwithstanding the provisions of Subsection (b) of this Section, bonds may be issued by any county in an amount not to exceed one-fourth of the assessed valuation of the real property in the county, for the construction, maintenance, and operation of macadamized, graveled, or paved roads and turnpikes, or in aid thereof, upon a vote of a majority of the voting qualified voters of the county, and without the necessity of further or amendatory legislation. The county may levy and collect taxes to pay the interest on the bonds as it becomes due and to provide a sinking fund for redemption of the bonds.

(d) Any defined district created under this section that is authorized to issue bonds or otherwise lend its credit for the purposes stated in Subdivisions (1) and (2) of Subsection (b) of this section may engage in fire-fighting activities and may issue bonds or otherwise lend its credit for fire-fighting purposes as provided by law and this constitution.

(e) A county, city, town, or other political corporation or subdivision of the state may invest its funds as authorized by law.

Article XI, Sec. 7. COUNTIES AND CITIES ON GULF OF MEXICO; TAX FOR SEA WALLS, BREAKWATERS, AND SANITATION; BONDS; CONDEMNATION OF RIGHT OF WAY.

(a) All counties and cities bordering on the coast of the Gulf of Mexico are hereby authorized upon a vote of the majority of the qualified voters voting thereon at an election called for such purpose to levy and collect such tax for construction of sea walls, breakwaters, or sanitary purposes, as may now or may hereafter be authorized by law, and may create a debt for such works and issue bonds in evidence thereof. But no debt for any purpose shall ever be incurred in any manner by any city or county unless provision is made, at the time of creating the same, for levying and collecting a sufficient tax to pay the interest thereon and provide at least two per cent (2%) as a sinking fund, except as provided by Subsection (b); and the condemnation of the right of way for the erection of such works shall be fully provided for.

(b) To increase efficiency and effectiveness to the greatest extent possible, the legislature may by general law authorize cities or counties to enter into interlocal contracts with other cities or counties without meeting the tax and sinking fund requirements under Subsection (a).

TAB 4 – RULE 15C2-12

(a) General. As a means reasonably designed to prevent fraudulent, deceptive, or manipulative acts or practices, it shall be unlawful for any broker, dealer, or municipal securities dealer (a “Participating Underwriter” when used in connection with an Offering) to act as an underwriter in a primary offering of municipal securities with an aggregate principal amount of $1,000,000 or more (an “Offering”) unless the Participating Underwriter complies with the requirements of this section or is exempted from the provisions of this section.

(b) Requirements.

(1) Prior to the time the Participating Underwriter bids for, purchases, offers, or sells municipal securities in an Offering, the Participating Underwriter shall obtain and review an official statement that an issuer of such securities deems final as of its date, except for the omission of no more than the following information: The offering price(s), interest rate(s), selling compensation, aggregate principal amount, principal amount per maturity, delivery dates, any other terms or provisions required by an issuer of such securities to be specified in a competitive bid, ratings, other terms of the securities depending on such matters, and the identity of the underwriter(s).

(2) Except in competitively bid offerings, from the time the Participating Underwriter has reached an understanding with an issuer of municipal securities that it will become a Participating Underwriter in an Offering until a final official statement is available, the Participating Underwriter shall send no later than the next business day, by first-class mail or other equally prompt means, to any potential customer, on request, a single copy of the most recent preliminary official statement, if any.

(3) The Participating Underwriter shall contract with an issuer of municipal securities or its designated agent to receive, within seven business days after any final agreement to purchase, offer, or sell the municipal securities in an Offering and in sufficient time to accompany any confirmation that requests payment from any customer, copies of a final official statement in sufficient quantity to comply with paragraph (b)(4) of this rule and the rules of the Municipal Securities Rulemaking Board.

(4) From the time the final official statement becomes available until the earlier of—

(i) Ninety days from the end of the underwriting period or

(ii) The time when the official statement is available to any person from the Municipal Securities Rulemaking Board, but in no case less than twenty-five days following the end of the underwriting period, the Participating Underwriter in an Offering shall send no later than the next business day, by first-class mail or other equally prompt means, to any potential customer, on request, a single copy of the final official statement.

(5)(i) A Participating Underwriter shall not purchase or sell municipal securities in connection with an Offering unless the Participating Underwriter has reasonably determined that an issuer of municipal securities, or an obligated person for whom financial or operating data is presented in the final official statement has undertaken, either individually or in combination with other issuers of such municipal securities or obligated persons, in a written agreement or contract for the benefit of holders of such securities, to provide the following to the Municipal Securities Rulemaking Board in an electronic format as prescribed by the Municipal Securities Rulemaking Board, either directly or indirectly through an indenture trustee or a designated agent:

(A) Annual financial information for each obligated person for whom financial information or operating data is presented in the final official statement, or, for each obligated person meeting the objective criteria specified in the undertaking and used to select the obligated persons for whom financial information or operating data is presented in the final official statement, except that, in the case of pooled obligations, the undertaking shall specify such objective criteria;

(B) If not submitted as part of the annual financial information, then when and if available, audited financial statements for each obligated person covered by paragraph (b)(5)(i)(A) of this section;

(C) In a timely manner not in excess of ten business days after the occurrence of the event, notice of any of the following events with respect to the securities being offered in the Offering:

(1) Principal and interest payment delinquencies;

(2) Non-payment related defaults, if material;

(3) Unscheduled draws on debt service reserves reflecting financial difficulties;

(4) Unscheduled draws on credit enhancements reflecting financial difficulties;

(5) Substitution of credit or liquidity providers, or their failure to perform;

(6) Adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701–TEB) or other material notices or determinations with respect to the tax status of the security, or other material events affecting the tax status of the security;

(7) Modifications to rights of security holders, if material;

(8) Bond calls, if material, and tender offers;

(9) Defeasances;

(10) Release, substitution, or sale of property securing repayment of the securities, if material;

(11) Rating changes;

(12) Bankruptcy, insolvency, receivership or similar event of the obligated person;

Note to paragraph (b)(5)(i)(C)(12): For the purposes of the event identified in paragraph (b)(5)(i)(C)(12) of this section, the event is considered to occur when any of the following occur: The appointment of a receiver, fiscal agent or similar officer for an obligated person in a proceeding under the U.S. Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the obligated person, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

(13) The consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material;

(14) Appointment of a successor or additional trustee or the change of name of a trustee, if material;

(15) Incurrence of a financial obligation of the obligated person, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the obligated person, any of which affect security holders, if material; and

(16) Default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the obligated person, any of which reflect financial difficulties; and

(D) In a timely manner, notice of a failure of any person specified in paragraph (b)(5)(i)(A) of this section to provide required annual financial information, on or before the date specified in the written agreement or contract.

(ii) The written agreement or contract for the benefit of holders of such securities also shall identify each person for whom annual financial information and notices of material events will be provided, either by name or by the objective criteria used to select such persons, and, for each such person shall:

(A) Specify, in reasonable detail, the type of financial information and operating data to be provided as part of annual financial information;

(B) Specify, in reasonable detail, the accounting principles pursuant to which financial statements will be prepared, and whether the financial statements will be audited; and

(C) Specify the date on which the annual financial information for the preceding fiscal year will be provided.

(iii) Such written agreement or contract for the benefit of holders of such securities also may provide that the continuing obligation to provide annual financial information and notices of events may be terminated with respect to any obligated person, if and when such obligated person no longer remains an obligated person with respect to such municipal securities.

(iv) Such written agreement or contract for the benefit of holders of such securities also shall provide that all documents provided to the Municipal Securities Rulemaking Board shall be accompanied by identifying information as prescribed by the Municipal Securities Rulemaking Board.

(c) Recommendations. As a means reasonably designed to prevent fraudulent, deceptive, or manipulative acts or practices, it shall be unlawful for any broker, dealer, or municipal securities dealer to recommend the purchase or sale of a municipal security unless such broker, dealer, or municipal securities dealer has procedures in place that provide reasonable assurance that it will receive prompt notice of any event disclosed pursuant to paragraph (b)(5)(i)(C), paragraph (b)(5)(i)(D), and paragraph (d)(2)(ii)(B) of this section with respect to that security.

(d) Exemptions.

(1) This section shall not apply to a primary offering of municipal securities in authorized denominations of $100,000 or more, if such securities:

(i) Are sold to no more than thirty-five persons each of whom the Participating Underwriter reasonably believes:

(A) Has such knowledge and experience in financial and business matters that it is capable of evaluating the merits and risks of the prospective investment; and

(B) Is not purchasing for more than one account or with a view to distributing the securities; or

(ii) Have a maturity of nine months or less.

(2) Paragraph (b)(5) of this section shall not apply to an Offering of municipal securities if, at such time as an issuer of such municipal securities delivers the securities to the Participating Underwriters:

(i) No obligated person will be an obligated person with respect to more than $10,000,000 in aggregate amount of outstanding municipal securities, including the offered securities and excluding municipal securities that were offered in a transaction exempt from this section pursuant to paragraph (d)(1) of this section;

(ii) An issuer of municipal securities or obligated person has undertaken, either individually or in combination with other issuers of municipal securities or obligated persons, in a written agreement or contract for the benefit of holders of such municipal securities, to provide the following to the Municipal Securities Rulemaking Board in an electronic format as prescribed by the Municipal Securities Rulemaking Board:

(A) At least annually, financial information or operating data regarding each obligated person for which financial information or operating data is presented in the final official statement, as specified in the undertaking, which financial information and operating data shall include, at a minimum, that financial information and operating data which is customarily prepared by such obligated person and is publicly available; and

(B) In a timely manner not in excess of ten business days after the occurrence of the event, notice of events specified in paragraph (b)(5)(i)(C) of this section with respect to the securities that are the subject of the Offering; and

(C) Such written agreement or contract for the benefit of holders of such securities also shall provide that all documents provided to the Municipal Securities Rulemaking Board shall be accompanied by identifying information as prescribed by the Municipal Securities Rulemaking Board; and

(iii) The final official statement identifies by name, address, and telephone number the persons from which the foregoing information, data, and notices can be obtained.

(3) The provisions of paragraph (b)(5) of this section, other than paragraph (b)(5)(i)(C) of this section, shall not apply to an Offering of municipal securities, if such municipal securities have a stated maturity of 18 months or less.

(4) The provisions of paragraph (c) of this section shall not apply to municipal securities:

(i) Sold in an Offering to which paragraph (b)(5) of this section did not apply, other than Offerings exempt under paragraph (d)(2)(ii) of this section; or

(ii) Sold in an Offering exempt from this section under paragraph (d)(1) of this section.

(5) With the exception of paragraphs (b)(1) through (b)(4), this section shall apply to a primary offering of municipal securities in authorized denominations of $100,000 or more if such securities may, at the option of the holder thereof, be tendered to an issuer of such securities or its designated agent for redemption or purchase at par value or more at least as frequently as every nine months until maturity, earlier redemption, or purchase by an issuer or its designated agent; provided, however, that paragraphs (b)(5) and (c) of this section shall not apply to such securities outstanding on November 30, 2010, for so long as they continuously remain in authorized denominations of $100,000 or more and may, at the option of the holder thereof, be tendered to an issuer of such securities or its designated agent for redemption or purchase at par value or more at least as frequently as every nine months until maturity, earlier redemption, or purchase by an issuer or its designated agent.

(e) Exemptive authority. The Commission, upon written request, or upon its own motion, may exempt any broker, dealer, or municipal securities dealer, whether acting in the capacity of a Participating Underwriter or otherwise, that is a participant in a transaction or class of transactions from any requirement of this section, either unconditionally or on specified terms and conditions, if the Commission determines that such an exemption is consistent with the public interest and the protection of investors.

(f) Definitions. For the purposes of this rule—

(1) The term authorized denominations of $100,000 or more means municipal securities with a principal amount of $100,000 or more and with restrictions that

prevent the sale or transfer of such securities in principal amounts of less than $100,000 other than through a primary offering; except that, for municipal securities with an original issue discount of 10 percent or more, the term means municipal securities with a minimum purchase price of $100,000 or more and with restrictions that prevent the sale or transfer of such securities, in principal amounts that are less than the original principal amount at the time of the primary offering, other than through a primary offering.

(2) The term end of the underwriting period means the later of such time as

(i) The issuer of municipal securities delivers the securities to the Participating Underwriters or

(ii) The Participating Underwriter does not retain, directly or as a member or an underwriting syndicate, an unsold balance of the securities for sale to the public.

(3) The term final official statement means a document or set of documents prepared by an issuer of municipal securities or its representatives that is complete as of the date delivered to the Participating Underwriter(s) and that sets forth information concerning the terms of the proposed issue of securities; information, including financial information or operating data, concerning such issuers of municipal securities and those other entities, enterprises, funds, accounts, and other persons material to an evaluation of the Offering; and a description of the undertakings to be provided pursuant to paragraph (b)(5)(i), paragraph (d)(2)(ii), and paragraph (d)(2)(iii) of this section, if applicable, and of any instances in the previous five years in which each person specified pursuant to paragraph (b)(5)(ii) of this section failed to comply, in all material respects, with any previous undertakings in a written contract or agreement specified in paragraph (b)(5)(i) of this section. Financial information or operating data may be set forth in the document or set of documents, or may be included by specific reference to documents available to the public on the Municipal Securities Rulemaking Board's Internet Web site or filed with the Commission.

(4) The term issuer of municipal securities means the governmental issuer specified in section 3(a)(29) of the Act and the issuer of any separate security, including a

separate security as defined in rule 3b–5(a) under the Act.

(5) The term potential customer means (i) Any person contacted by the Participating Underwriter concerning the purchase of municipal securities that are intended to be offered or have been sold in an offering, (ii) Any person who has expressed an interest to the Participating Underwriter in possibly purchasing such municipal securities, and (iii) Any person who has a customer account with the Participating Underwriter.

(6) The term preliminary official statement means an official statement prepared by or for an issuer of municipal securities for dissemination to potential customers prior to the availability of the final official statement.

(7) The term primary offering means an offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities, including any remarketing of municipal securities.

(i) That is accompanied by a change in the authorized denomination of such securities from $100,000 or more to less than $100,000, or

(ii) That is accompanied by a change in the period during which such securities may be tendered to an issuer of such securities or its designated agent for redemption or purchase from a period of nine months or less to a period of more than nine months.

(8) The term underwriter means any person who has purchased from an issuer of municipal securities with a view to, or offers or sells for an issuer of municipal securities in connection with, the offering of any municipal security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; except, that such term shall not include a person whose interest is limited to a commission, concession, or allowance from an underwriter, broker, dealer, or municipal securities dealer not in excess of the usual and customary distributors' or sellers' commission, concession, or allowance.

(9) The term annual financial information means financial information or operating data, provided at least annually, of the type included in the final official statement with respect to an obligated person, or in the case where no financial information or operating data was provided in the final official statement with respect to such obligated person, of the type included in the final official statement with respect to those obligated persons that meet the objective criteria applied to select the persons for which financial information or operating data will be provided on an annual basis. Financial information or operating data may be set forth in the document or set of documents, or may be included by specific reference to documents available to the public on the Municipal Securities Rulemaking Board's Internet Web site or filed with the Commission.

(10) The term obligated person means any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund, or account of such person committed by contract or other arrangement to support payment of all, or part of the obligations on the municipal securities to be sold in the Offering (other than providers of municipal bond insurance, letters of credit, or other liquidity facilities).

(11)(i) The term financial obligation means a:

(A) Debt obligation;

(B) Derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation; or

(C) Guarantee of paragraph (f)(11)(i)(A) or (B).

(ii) The term financial obligation shall not include municipal securities as to which a final official statement has been provided to the Municipal Securities Rulemaking Board consistent with this rule.

(g) Transitional provision. If on July 28, 1989, a Participating Underwriter was contractually committed to act as underwriter in an Offering of municipal securities originally issued before July 29, 1989, the requirements of paragraphs (b)(3) and (b)(4) shall not apply to the Participating Underwriter in connection with such an Offering. Paragraph (b)(5) of this section shall not apply to a Participating Underwriter that has contractually committed to act as an underwriter in an Offering of municipal securities before July 3, 1995; except that paragraph (b)(5)(i)(A) and paragraph (b)(5)(i)(B) shall not apply with respect to fiscal years ending prior to January 1, 1996. Paragraph (c) shall become effective on January 1, 1996. Paragraph (d)(2)(ii) and paragraph (d)(2)(iii) of this section shall not apply to an Offering of municipal securities commencing prior to January 1, 1996.

TAB 5 – SOURCES FOR FURTHER READING

Attorney General of Texas, Public Finance Division –
https://www.texasattorneygeneral.gov/divisions/public-finance

Site contains useful information about transcript requirements and the attorney general review process.

Electronic Municipal Market Access (EMMA) – https://emma.msrb.org/

The repository of municipal bond offering documents maintained by the Municipal Securities Rulemaking Board. This site includes access to offering documents.

Government Finance Officers Association – https://www.gfoa.org/

Website includes many resources related to the issuance of debt, including statements of best practices.

Municipal Securities Rulemaking Board, Glossary –

http://www.msrb.org/glossary.aspx

The Municipal Securities Rulemaking Board (MSRB) site has many useful resources. The glossary of municipal securities terms is comprehensive and typically up to date.