# *Bonds and Certificates of Obligation: Funding Options for Roads*

**4.001 Bonds and Certificates of Obligation**

**South Texas County Judges and Commissioners**

**Association Conference**

Tuesday, June 12, 2018

2:10 PM

Presented By:


**David Méndez, Partner**

Bickerstaff Heath Delgado Acosta LLP

3711 South Mopac Expressway

Building One, Suite 300

Austin, Texas 78746

P: 512-472-8021 F: 512-320-5638

# OBJECTIVES

- Provide a brief overview of the finance vehicles available to Texas counties with a focus on funding road projects
- Identify key issues on which the commissioners court should focus when issuing bonds
- Review special aspects of funding road projects

# FIRST: A LITTLE BACKGROUND

- Things to line out before you start:
  - Clarify the court’s needs and objectives
    - Why is this project needed?
    - Can we afford it (how will we pay for it)?
    - Will the community support it?
  - Discuss your needs and objectives with your financial team
    - Financial Advisor
    - Bond Counsel

# Team Members

- **County's Financial Advisor**
  - The professional who will guide the county through the economic side of the issuance process
  - The professional who will evaluate the economics of different financing structures and recommend the type of issue to be used – G.O. Bonds, CO's, Anticipation Notes, etc.
  - The professional who will conduct the competitive sale or negotiated sale or arrange for a private placement

# Team Members

- **County's Bond Counsel**
  - The county's lawyer in the transaction who will advise you on and prepare the financing documents
  - Provides the "Bond Opinion" which opines that the obligations were properly issued and if issued on a tax exempt basis, that the obligations are not subject to federal income taxation
  - Must know local government law, federal tax law and securities law
  - An Attorney-Client relationship must exist between the county and the county's bond counsel
  - The county has the right to select its own bond counsel

# BEGINNING THE PROCESS

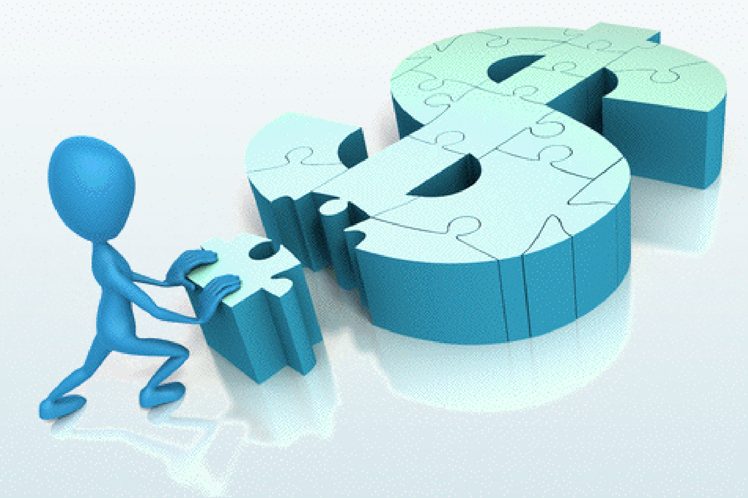
**Topics to discuss with your team:**

- What is the size, scope, and timing of your project?
- How does this project and the financing fit in with the County's existing debt service?
- How does this project fit in with the County's Capital Improvement Plan?

# Bonds for Transportation Projects

# FINANCING METHODS

- **General Obligation Bonds**
- **Certificates of Obligation**
- **Lease-Purchase Contracts**
- Contractual Obligations
- Anticipation Notes
- Time Warrants
- Public Improvement District Bonds
- Revenue Bonds



# What About a Financing Lease or Installment Purchase Contract?

- Viable option for some road building equipment needs, but may or may not constitute an obligation that can be classified as a debt for ad valorem tax purposes.

- If characterized as an M&O obligation, no relief from roll back.

# GENERAL OBLIGATION BONDS ("Unlimited Tax G.O. Bonds")Chap 1471

| | |
|---|---|
| Election: | Yes |
| Pledge: | Ad Valorem Tax |
| Typical Use: | Major capital projects where the commissioners court believes that it is important to have the voters approve the project |
| Max Term: | 40 Years (Typically 15-20) |
| Requirements: | Posting/Publication, etc. |

# Specific Road Bond Authority

- Tex. Govt. Code Chapter 1471
- Tex. Govt. Code Chapter 1479
- Tex. Govt. Code Chapter 1301
- Tex. Transp. Code Chapter 256

# Unlimited Tax Road Bonds (Other Bonds under Chapter 1471)

- Road District Bonds
- Precinct Bonds
- Bond Anticipation Bonds

# PASS-THROUGH TOLL BONDS
# Chapter 1479 Bonds

- Not currently funded.
- Initially created in 2005, -- counties have been authorized to issue "pass-through toll revenue and tax bonds" to fund highway projects that are part of the state highway system, which includes farm-to-market roads. In 2003, the legislature enacted Section 224.104 of the Texas Transportation Code which authorized the Texas Department of Transportation (the "Department") to use a new method of paying for highway projects, known as the "pass-through toll".

# CERTIFICATES OF OBLIGATION ("C.O.s")

| | |
|---|---|
| Election: | 5% of Voters May Petition |
| Pledge: | Ad Valorem Tax, Revenue, or Combination |
| Typical Use: | Capital projects where an election not viewed as necessary |
| Max Term: | 40 Years (Typically 15-20) |
| Requirements: | Posting/Publication, etc. |

# ANTICIPATION NOTES ("Tax Notes")

| | |
|---|---|
| Election: | No |
| Pledge: | Ad Valorem Tax, Revenue, or Combination |
| Typical Use: | Construction of a public work; purchase of materials, supplies, equipment, machinery, buildings, lands, and rights-of-way; professional services such as engineers, architects, attorneys and financial advisors; operating expenses; or to fund issuer's cumulative cash flow deficit |
| Max Term: | 7 Years (1 Year for Cash Flow Deficit) |
| Requirements: | Auditor's recommendation (or Chief Budget Officer) |

# CONTRACTUAL OBLIGATIONS

| | |
|---|---|
| Election: | No |
| Pledge: | Ad Valorem Tax, Revenue, or Both |
| Typical Use: | For Personal Property Only |
| Max Term: | 25 Years |
| Requirements: | None |

# PUBLIC IMPROVEMENT DISTRICT BONDS ("PID BONDS")

| | |
|---|---|
| Election: | No (Landowner Petitions In) |
| Pledge: | Special Assessment |
| Typical Use: | Roads, utilities and related subdivision infrastructure in a specific subdivision |
| Max Term: | 40 Years (But Typically Shorter) |
| Requirements: | District Creation, Posting/Publication, etc. |

# UNLIMITED TAX ROAD DISTRICT BONDS ("Road District Bonds")

| | |
|---|---|
| Election: | Yes (Within Defined District) |
| Pledge: | Ad Valorem Tax |
| Typical Use: | Roads, bridges and similar improvements in a specific defined district |
| Max Term: | 40 Years (But Typically Shorter) |
| Requirements: | District Creation, Posting/Publication, etc. |

# REVENUE BONDS

| | |
|---|---|
| Election: | No |
| Pledge: | County Revenues from Public Utility (solid waste, library, etc.) |
| Typical Use: | Rarely available to counties; used more by cities and utility districts |
| Max Term: | 40 Years (Typically 15-20) |
| Requirements: | Coverage |

# TIME WARRANTS

| | |
|---|---|
| Election: | Subject to Voter Petition |
| Pledge: | Ad Valorem Tax |
| Typical Use: | Older Method of Finance Authorized under Chapter 262 of the Texas Local Government Code |
| Max Term: | 40 years |
| Requirements: | Time Warrants are Subject to Publication Requirements & Non-Negotiable |

# TIME WARRANTS

- Disadvantages:
  - Time Warrants are non-negotiable instruments
  - Time Warrants may not be sold for cash
  - Consequently, arrangements must be made with a vendor to accept the time warrant and a bank to buy the time warrant from the vendor

# TIME WARRANTS


- Disadvantages:
  - Time warrants often are prepared locally. As a consequence, there may not be all the formalities taken to ensure that the time warrant is a tax-exempt obligation.
    - The rates charged may be higher than market for a tax-exempt security
    - The time warrant may be for beyond one fiscal year, and the formality of an interest and sinking fund may not be established. This will render the time warrant invalid.

# LEASE PURCHASE AGREEMENT/ INSTALLMENT SALES CONTRACT

- Permits the county to purchase goods over period of time
- Is not a pledge of taxes
  - Unless for equipment and properly structured
- Is a maintenance and operations expense, not a debt service expense
- Attorney General approval is not required

# LEASE PURCHASE AGREEMENT/ INSTALLMENT SALES CONTRACT

- Must be subject to annual appropriations
- No requirement to continue
- Practical limits on the ability to discontinue
- Interest rates are often higher than a tax obligation

# REFUNDING BONDS

- Used to refinance the county's outstanding bonds and other obligations
- Allows county to take advantage of lower interest
- Used to restructure debt payments
- No newspaper publication requirement
- No election requirement

# TEXAS LAW CHANGES

- Bond Election Dates
- Limitation on holding bond elections
- Additional notice requirements for bond elections

# Bond Election Dates

- Uniform Election dates are now limited to:
  - First Saturday in May of odd-numbered years
  - First Tuesday after first Monday in November
- Counties cannot hold bond elections in May of even-numbered years because of primaries.

# Limitation on Holding Bond Elections

***Effective January 1, 2016***

County may not authorize COs if a bond proposition to authorize the issuance of bonds for the same purpose was submitted to the voters during the preceding three years and failed to be approved.

***Exceptions***

- Public calamity
- To comply with court order/regulation

# The County's Duties Do Not End When the Bonds are Issued

- You **MUST** comply with requirements you promised in the bond documents that you would not let the bonds become taxable
- What may cause the problem – **TURNOVER**
- The personnel that were there when the bonds were issued have departed before the bonds are paid off
- You need to familiarize yourself with the requirements so that you can brief your successors

# Resources:

2017
PUBLIC FINANCE HANDBOOK
FOR TEXAS COUNTIES

TEXAS ASSOCIATION OF COUNTIES
1210 San Antonio Street Austin, Texas 78701

**Honorable Joyce Hudman**
*Brazoria County Clerk & Association President*

**Gene Terry**
*Executive Director*

**Rex Hall**
*Assistant Executive Director*

PREPARED BY THOMAS M. POLLAN & DAVID MÉNDEZ
BICKERSTAFF HEATH DELGADO ACOSTA, LLP
3711 SOUTH MOPAC EXPRESSWAY
BUILDING ONE, SUITE 300
AUSTIN, TEXAS 78746
(512) 472-8021

LEGAL RESEARCH
Legal Helpline: (888) 275-8224 • Toll Free: (800) 456-5974
or visit our website at www.county.org

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- http://www.bickerstaff.com/wp-content/uploads/2017-Public-Finance-Final.pdf
- http://www.bickerstaff.com/publications/

# Resources:

- [http://www.mazdigital.com/webreader/51105?page=14](http://www.mazdigital.com/webreader/51105?page=14)
- Article in *County Progress*

## Financing Routine Capital Expenditures

Each year as counties prepare their budgets, along with the routine maintenance and operational costs, counties inevitably face the need to budget for some routine capital items. Law enforcement vehicles or road grading equipment may need replacement; radios, computers or office equipment may have worn out; gravel and road base material may be needed to repair county roads; or the courthouse roof may need patching. All of these are, technically, capital expenditures – that is, they can benefit the county over a period of time. While financing these items over a period that matches the useful life is possible, many times the county acquires these items by simply paying cash for the items as part of the annual budget or by leasing.

Two problems arise from such treatment. First, to the extent the entire cost of the item is paid for in one budget year, taxpayers incur a disproportionate cost in the current year for the item which ultimately benefits potentially different taxpayers in later years. Second, to the extent the county leases the item or acquires it through a lease purchase arrangement, there are built-in transaction costs in each lease or lease purchase agreement, and the cumulative cost of those individual purchases will be much more expensive than if the county financed all of the capital items it needs for the year with one transaction.

Some counties have used tax notes to consolidate the acquisition of all of these capital items during a year with one loan. This has allowed the county to reduce its M&O costs and realize the benefit of more efficient (cheaper) transaction costs for buying these items. Counties typically implement the program in the following manner: At the time the county sets the budget, it identifies all of the eligible capital items. Then it can issue one tax note at the beginning of the year to pay for these items as needed


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