



**House
Legislative
Analysis
Section**

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**LIMITED TAX OBLIGATION BONDS:
NOTICE AND REFERENDUM**

**House Bills 4885-4888 (Substitutes H-3)
House Bill 4890 (Substitute H-3)
House Bills 4892-4902 (Substitutes H-3)
House Bills 4904-4911 (Substitutes H-3)
First Analysis (10-18-01)**

**Sponsor: Rep. John Pappageorge
Committee: Tax Policy**

THE APPARENT PROBLEM:

According to municipal finance specialists, tax obligation bonds issued by municipalities fall, generally speaking, into two categories: unlimited and limited. Unlimited tax obligation bonds pledge the unlimited full faith and credit of the municipality and are backed by the ability of the municipality to raise taxes if necessary to meet its obligations. They require voter approval before being issued. Limited tax obligation bonds do not commit the municipality to raise additional taxes but are to be repaid out of current voter-approved millage rates. This second kind of bond can be issued by the governing body without a vote of the electorate and without the publication of any legal notice of the intent to issue them. (However, city charter provisions may require notice, according to the Michigan Municipal League.) The limited tax general obligation bonds are said to have become increasingly popular since the passage of the Headlee Amendment of 1978, which required tax obligation bonds that could increase taxes to be put before voters. Critics of limited tax general obligation bonds believe they ought to be subject to notice requirements so that local taxpayers are aware of them and, can if they desire, file petitions and subject the bond issues to referendum. They point out that while bondholders cannot not force a local unit of government to raise taxes to meet the limited tax obligation bond payments, they can empty the local treasury (and, some would argue, force future tax increases). Taxpayers at least ought to be informed in advance of a municipality's intention to issue such debt. Critics point to one celebrated case in which a local school board, after twice failing to pass an unlimited tax obligation bond issue to build a new high school, instead issued limited tax obligation bonds, which the district was able to do because it was not levying all of the mills it was authorized to levy. This was seen as an affront to local taxpayers, and reportedly all but one of the school board members were recalled.

The legislature recently enacted a Revised Municipal Finance Act, which takes effect in March of 2002. That act, which generally governs municipal borrowing and the issuance of debt, allowed for a new kind of long-term bond called a "budget bond". A local unit could finance capital improvements by issuing bonds to be paid for out of its operating budget. Such bonds could not require the municipality to raise taxes to pay principal and interest. The section that addresses these bonds, Section 517, says that before a local unit can issue the bonds, it must publish a notice of its intent to issue them in a newspaper of general circulation and notify the voters of their right of referendum on the bonds. The section spells out what needs to be done to force a referendum. Legislation has been introduced that would make the provisions regarding the notice of intent and right of referendum found in Section 517 apply to all limited tax obligation bonds.

THE CONTENT OF THE BILLS:

Under the bills, generally speaking, if a local governmental unit or any of a variety of authorities issued a limited tax obligation bond that was a municipal security under the Revised Municipal Finance Act, the issuing entity would have to publish a notice of intent to issue the bonds. Further, voters could then petition for a referendum on the bond issue. Each of the bills in the 24-bill package would amend a different act under which such bonds are issued. (The bills would not apply to an unlimited tax obligation bond, a revenue bond, or a refunding bond.) The bills would take effect March 1, 2002.

Each of the bills would make limited tax obligation bonds subject to the notice and referendum requirements already found (at Section 517) in the Revised Municipal Finance Act for so-called budget bonds. These are long-term capital improvement

House Bills 4885-4888, 4890, 4892-4902 and 4904-4911 (10-18-01)

bonds that a county, city, village, or township can issue by resolution of its governing body and without a vote of its electors, provided the amount of taxes necessary to pay the principal and interest, together with other taxes levied, would not exceed authorized limits. The Revised Municipal Finance Act (Public Act 34 of 2001), including Section 517, takes effect on March 1, 2002.

Notice of Intent. The notice of intent, which would have to be at least one-quarter page in size in the newspaper, would be directed to the voters of the municipality, be published in a newspaper that had a general circulation in the municipality, and would have to state the maximum amount of bonds to be issued, the purpose of the bonds, the source of payment, the right of referendum on the bonds, and other information the local governing body determined necessary to adequately inform the voters of the nature of the issue.

Right to Referendum. The bonds would be subject to a referendum before being issued if, within 45 days after the publication of the notice of intent, a petition signed by at least 10 percent of registered electors or 15,000 registered electors, whichever was less, was filed with the local governing board requesting a referendum. (The local governing board would determine the number of registered voters in the municipality.) The bonds could only be issued if approved by a majority vote at a general or special election. A special election called for this purpose would not be included in a statutory or charter limitation as to the number of special elections that can be called within a period of time. Petition signatures would be verified by a person under oath as the actual signatures of the persons whose names were signed to the petition, and the local governing body would have the same power to reject signatures and petitions as city clerks do under the Home Rule City Act.

Municipal security. The Revised Municipal Finance Act defines "municipal security" as a security that when issued is not exempt from the act or the old Municipal Finance Act or from the act under which it was issued and that is payable from or secured by 1) ad valorem real and personal property taxes; 2) special assessments; 3) the limited or unlimited full faith and credit pledge of the municipality; and 4) other sources of revenue described in the act for debt or securities authorized by the act.

House Bill 4885 would amend Public Act 175 of 1952 (MCL 247.701a) dealing with borrowing by

cities and villages from the motor vehicle highway fund.

House Bill 4886 would amend the Downtown Development Authority Act (MCL 125.1666a).

House Bill 4887 would amend Public Act 143 of 1943 (MCL 141.251a) empowering county boards of commissioners to borrow for road machinery or equipment or road improvement.

House Bill 4888 would amend Public Act 246 of 1931 (MCL 41.283b) addressing sidewalk and pavement improvements.

House Bill 4890 would amend the Drain Code (MCL 280.274a).

House Bill 4892 would amend Public Act 156 of 1851 (MCL 46.11d) dealing with county commissioners.

House Bill 4893 would amend the Brownfield Redevelopment Financing Act (MCL 125.2667a).

House Bill 4984 would amend Public Act 344 of 1945 (MCL 125.77d) addressing the rehabilitation of blighted areas by counties, cities, villages, and townships.

House Bills 4895 would amend Public Act 188 of 1954 (MCL 41.735d) dealing with township improvements.

House Bill 4896 would amend the Home Rule Village Act (MCL 78.24d).

House Bill 4897 would amend the Home Rule City Act (MCL 117.5j).

House Bill 4898 would amend the General Law Village Act (MCL 61.35a).

House Bill 4899 would amend Public Act 233 of 1955 (MCL 124.289a) addressing municipal sewer, water, and solid waste systems.

House Bill 4900 would amend the Charter Township Act (MCL 42.14b).

House Bill 4901 would amend the County Public Improvement Act (MCL 46.175d).

House Bill 4902 would amend Public Act 208 of 1949 (MCL 125.946d) dealing with neighborhood blight prevention.

House Bill 4904 would amend the Fourth Class City Act (MCL 81.19a).

House Bill 4905 would amend the Community College Act (MCL 389.122b).

House Bill 4906 would amend the Revised School Code (MCL 380.629a) to address certain bonds issued by intermediate school districts and local school districts.

House Bill 4907 would amend the Shopping Areas Redevelopment Act (MCL 125.985a).

House Bill 4908 would amend the Public Transportation Authority Act (MCL 124.473a).

House Bill 4909 would amend the Tax Increment Finance Authority Act (MCL 125.1812b).

House Bill 4910 would amend Public Act 31 of the Extra Session of 1948 regarding buildings, parking lots, stadiums, and recreational facilities owned, operated, and maintained by special authorities (MCL 123.9611).

House Bill 4911 would amend Public Act 185 of 1957 (MCL 123.741 and 123.741a) dealing with county public works departments.

BACKGROUND INFORMATION:

The Revised Municipal Finance Act (Public Act 34 of 2001) is described in the Senate Fiscal Agency's analysis of Senate Bill 29 dated 8-7-01 and in an analysis of the same bill by the House Legislative Analysis Section dated 6-5-01.

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that the bills could increase local administrative costs by an indeterminately small amount, and would have no direct state fiscal impact. (HFA fiscal note dated 10-15-01)

ARGUMENTS:

For:

Municipalities do not have to seek voter approval before issuing limited tax obligation bonds. The apparent justification for this is that, unlike unlimited tax obligation bonds, they do not carry with them the ability to make a municipality raise taxes to meet its bond payments. Limited tax obligation bonds only

pledge existing statutorily voted millage. But, of course, such bond issues can affect future tax levels. Critics say the use of these bonds can lead to abuses by local units of government and the disenfranchisement and disillusionment of voters, who do not even have to be informed by a published notice of the unit's intent to issue debt backed by the local treasury. This package of bills would require that the public be notified and would allow taxpayers the ability to put limited tax obligation bonds before the voters at referendum. The growth of the use of limited tax obligations since the passage of the Headlee Amendment in 1978 is seen in some quarters as a way for local governmental units to avoid putting debt before the voters, as that constitutional amendment had intended for general obligation bonds. This package of bills would still allow municipalities to issue limited tax obligation bonds without a vote of the people, but requires that there be prior public notice of the intent to issue bonds and allows the public to subject the bonds to referendum. This is consistent with the philosophy that increases in taxes and in bonded indebtedness should be subject to voter approval.

Response:

Municipal finance specialists say that this legislation represents a substantial broadening of notice requirements and of the right to referendum. Is this necessary when only a handful of the great many limited tax obligation bond issues each year creates any controversy? There are hundreds of these bond issues each year, which means there will have to be a lot of quarter-page notice advertisements. In instances where a right of referendum already exists, according to bond specialists, fewer than one-half of one percent of proposed bond issues result in petitions for a referendum. The great increase in the number of notices to be published will increase the cost of issuing bonds. That alone could discourage some communities, and in particular smaller communities, from proceeding. Perhaps there should be a threshold size of a bond issue before the requirement applies. Further, the pledge of limited full faith and credit is often a secondary security; that is, transportation bonds or special assessment bonds are issued with the expectation that a certain stream of revenue will be used to repay the bonds, but as a secondary measure, the local unit backs up that revenue with a pledge of its existing millage. This results in significantly lower interest costs, say bond experts, and a thus a savings to municipalities. If bonds are issued without that secondary security, to avoid these new requirements, there will be increased borrowing costs. Perhaps different requirements should be applied in these cases. Representatives of local units point out that there is no right of

referendum for appropriations, or on long-term leases, or on revisions to assumptions in pension plans, all of which can have implications for future tax rates. With limited tax obligation bonds, the local unit pledges only currently voted millage rates and cannot raise taxes beyond the level already approved by voters.

POSITIONS:

The Michigan Townships Associations is supportive of the bills but has questions. (10-17-01)

The Michigan Municipal League has no position on the bills. (10-17-01)

Analyst: C. Couch

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.