

POLITICAL SUBDIVISION BONDING QUESTIONS

September 5, 2007

We have been asked to provide comment for the committee's consideration regarding the following issues.

1. *Legal or market-based limits on special assessment debt.*

- There is no legal limit on the amount of special assessment debt that an issuer can incur. Any market limit on the sale of special assessment bonds would be based on the general credit status of the issuer.
- Issuers are required to back special assessment bonds with their general obligation credit (deficiency levy). The North Dakota Supreme Court in *Marks v. Mandan*, 296 N.W. 39 (1941), ruled that the pledge of the issuer's general obligation credit was contingent debt and did not count against the issuer's debt limit until there was a short-fall in the payment of bond debt service. (The City of Belfield financed infrastructure improvements such as water and sewer for a trailer park that did not pay the special assessments.)

2. *How are bond ratings obtained and what difference do ratings make to the interest rate?*

- A rating is obtained by the issuer or underwriter making application to one of the nationally recognized rating agencies (Moody's, Standard & Poor's and Fitch). The issuer provides financial information to the rating agency, pays their fee and the rating agency decides whether or not it will rate the bonds and what the rating will be.
- Rated bonds usually have a lower interest rate because an independent third party has reviewed the financial soundness of the transaction, and rated bonds have easier access to the secondary market.

3. *Building authority's used to issue bonds and build facilities without a vote of the electors.*

- Federal law allows a corporation organized under the general nonprofit corporation law of a state to issue tax-exempt bonds for the benefit of a political subdivision. These types of transactions are known as "63-20" financings after the Internal Revenue Service Revenue Ruling recognizing such transactions.
- School districts, park districts, cities and counties have used 63-20 financings through a corporation called a building authority. In a building authority financing, the nonprofit corporation issues bonds to construct facilities on behalf of governmental entities. The governmental entities use the facilities on an annual lease basis.
- A vote of the electors is not required because no debt is incurred in the constitutional sense. No additional tax levy is imposed and the annual lease rentals are budgeted and paid out of the political subdivision's general fund. The holders of the bonds of the building authority run the risk of the political subdivision not appropriating funds to pay the lease rentals. There is no recourse against the political subdivision by the bondholders.