

Municipal Finance Basics

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Municipal Finance Basics

Governing Law

- The Constitution of the State of New York
- New York Local Finance Law
- Town Law/Village Law/General City Law/County Law
- Internal Revenue Code
- SEC Regulations

Types of Borrowings Allowed

- **Serial Bonds**
- Statutory Installment Bonds (\$5 million max)
- **Bond Anticipation Notes (BAN)**
- Tax Anticipation Notes (TAN)
- Revenue Anticipation Notes (RAN)
- Others, rarely seen

Types of Borrowings Allowed

- Lease-Purchase Financing for Equipment
 - Typically more expensive
- **No traditional bank loans allowed**

Financing Municipal Projects

Five phases:

1. Planning
2. **AUTHORIZATION**
3. Short-Term Financing (BAN)
4. Long-Term Financing (Bonds)
5. Post-Issuance Compliance (Tax/Continuing Disclosure)

Planning for Municipal Financing

State Environmental Quality Review Act (“SEQRA”) Compliance

- Municipality must consider environmental impact of every project.
- Large projects may require “coordinated review” with other involved agencies.
- **Bond resolution cannot be adopted until SEQRA is complete.**
- Typically handled by engineers.

Planning for Municipal Financing

Bond Maturity Schedule

- Maximum maturity cannot exceed the “period of probable usefulness” (PPU) computed from date of first borrowing.
 - **Local Finance Law Section 11** - PPU for laundry list of projects.

Planning for Municipal Financing

Bond Maturity Schedule

- Public Policy: cannot back-load debt payments.
- First principal installment within two years of first borrowing.
- Two allowable amortization methods
 - fifty percent (50%) rule
 - substantially level or declining total annual debt service
- Financial Advisor will help with this.

Authorization of Bonds and BANs

The Bond Resolution

- Specific language required by Local Finance Law Sections 31 and 32.
 - Bond counsel prepares bond resolution.
- Must be approved by two-thirds of the entire Board
 - Vacant seats are not disregarded.
 - Example: Five person board, one vacancy - four out of four vote is required.
- Roll call vote is required

Authorization of Bonds and BANs

Permissive Referendum Requirement

- City and County bond resolutions are generally not subject to permissive referendum
- Town/Village bond resolutions are subject to permissive referendum, with some exceptions, including:
 - If maximum maturity is 5 years or less
 - Special district improvements (Towns)
 - Payment of judgments or compromised or settled claims

Authorization of Bonds and BANs

Permissive Referendum Process

- Within ten days after resolution adopted, post and publish “Notice of Adoption of Resolution Subject to Permissive Referendum”.
 - Bond counsel prepares this notice.
 - Publish in Municipalities’ Official Newspaper.
 - Post on Official Sign Board, and on Municipal website maintained for legal notices.

Authorization of Bonds and BANs

Permissive Referendum Process

- Town-wide/Village-wide referendum required if Clerk receives a valid petition signed by qualified voters equal to **five percent (5%) of total votes cast in the Municipality for governor in the last general election.**
 - Hold referendum within 60-75 days after petition received.
- If no petition is received, bond resolution is effective 30 days after *adoption.*

Authorization of Bonds and BANs

Estoppel Notice

- Publish bond resolution, or a summary, with specific notice language.
 - Bond counsel will prepare Estoppel Notice.
- Publish one time in official newspaper.
 - Publish **after** 30 day permissive referendum period, if applicable.
- Prevents most legal challenges to borrowing.

Temporary Financing

Bond Anticipation Notes (BANs)

- Up to one year maturity, and may then be renewed (refinanced).
- Interest paid at maturity.
- Principal reduction from current funds required after two years.
 - Specific requirements for principal amortization (50% rule or level total debt service).
- BAN renewals generally limited to five years max.
 - Exception for special improvement district financing.

Sale of BANs/Bonds

Public vs. Private Sale

- BANs may be sold at private, negotiated sale.
 - Larger issues typically sold at public sale to get best rates.
- Bonds must generally be sold at public sale on a competitive basis to the lowest bidder.
 - Bonds up to \$5 million may be sold at private negotiated sale.
- Should still solicit bids if negotiated (non-public) sale, to get best interest rate.

Sale of Bonds

Conducting a Public Sale

- Publish “Notice of Sale” in various places.
- Prepare and distribute “Official Statement”
- Financial Advisor typically prepares and distributes Notice of Sale and Official Statement.

Sale of Bonds

Official Statement

- Required under federal securities law for bonds greater than \$1 million.
 - Some exceptions
- Detailed information regarding Municipality and its financial condition, including tax and budget figures for the last five fiscal years.
- **Federal securities law – must be no material inaccuracies or omissions.**

Sale and Delivery of Bonds

The Bond Closing

- Bond/BAN certificates and other closing documents are signed by appropriate town officials.
- Bond Counsel handles the closing
- Larger bond/BAN issues – Depository Trust Company (DTC) holds the bonds on behalf of investors.

Post Issuance Compliance

- Continuing Disclosure Compliance
- Tax Compliance

Continuing Disclosure Compliance

- At closing of public bond or BAN issue, the municipality signs **“Continuing Disclosure Agreement”** that requires:
 - **Posting annual financial information on “EMMA”** (Electronic Municipal Market Access) System.
 - **Posting notice of specific events** if they occur:
 - Payment defaults
 - Rating changes
 - Incurrence of financial obligation (i.e., additional debt)
 - Other specific events
- Exceptions for smaller issuers/issues.
- Financial Advisor typically helps with continuing disclosure filings.

Tax Compliance

- Two primary areas:
 - Private business use
 - Arbitrage
- Failure to comply with tax law requirements can cause interest on bonds/BANs to be taxable.
 - Municipality would be liable to bondholders, or IRS, for taxes, penalties and interest.
- Maintain detailed records regarding expenditure of bond/BAN proceeds until 3 years after debt repaid.

Tax Compliance

Private Business Use Limitations

- No more than 10% of bond proceeds may be used for private business use.
- Measured based on use of bond-financed facilities.

Tax Compliance

Examples of private business use:

- Sale of bond-financed facility.
- Lease of space in bond-financed facility to non-governmental entity.
- Facility management contracts (e.g., food service at public arena), unless meet certain requirements.
- Contracts granting priority rights to private business (e.g., reserved parking spaces in parking garage), unless meet certain requirements.

Tax Compliance

Examples of use that is **not** private business use:

- Use by the general public.
- Use by individuals not engaged in trade or business.
- Use at prices that are generally applicable and uniformly applied.
- Certain negotiated short-term arrangements (50-100 days) may also be permitted.

Tax Compliance

Arbitrage Restrictions

- Arbitrage bonds are not tax-exempt.
- “Arbitrage”: amount earned on investment of bond/BAN proceeds in excess of amount that would be earned if proceeds invested at bond/BAN yield.
- Example: BAN issued at 3% interest rate; proceeds invested to earn 4%.
- Several exceptions, including three year “temporary period” exception for construction financing.

Tax Compliance

Arbitrage Rebate

- Arbitrage earned during permitted “temporary period” must be paid to IRS.
- Arbitrage rebate calculation required every five years during the bond term, and within 60 days after final bond payment.
- Several exceptions to arbitrage rebate requirement.

Tax Compliance

Arbitrage Rebate Exceptions

- Small Issuers (\$5 million of debt in current year).
- Six month spend-down exception.
- 18 month spend-down exception.

Any Questions?

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