BOND FINANCING HANDBOOK FOR INDIANA MUNICIPAL OFFICIALS

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PART I.

CITY AND TOWN FINANCINGS: IN GENERAL

CHAPTER 1.
FINANCINGS FOR MUNICIPAL PROJECT AND PURPOSES

A municipal financing is simply a transaction in which the city or town borrows money for a public project or purpose and enters into a contract in which the city or town agrees to repay the loan, on a certain repayment schedule, at an agreed interest rate, and from an agreed repayment source (for example, from revenues of a utility, or from property taxes).

The loan transaction is accomplished by issuing and selling a "bond," which is in essence a promissory note.

Municipal officials may assume that borrowing money is something that should be avoided at all costs. However, issuing long-term debt is often very necessary, and undue reluctance will not serve constituents in the long run. Long-lifed municipal assets are essential to local government, and it is not unreasonable that the cost of a building that will last for 20+ years should be paid for by future users in addition to current users.

As the leaders and policymakers of your municipality, it is your right (and duty) to prioritize the needs of your city or town. It is the job of your local attorney, in concert with your municipal advisor and bond counsel, to assist you with evaluating how best to achieve your objectives.

The purpose of the handbook is to help you achieve your goals and better serve your constituents by providing you with a (hopefully) plain-language, non-"legalese" overview of Indiana municipal finance.

CHAPTER 2. GLOSSARY OF TERMS

Concepts and terms that are common in municipal financing include the following.

"2019 pay 2020" means taxes payable during 2020, for which the tax liability is determined based on who the owner was on January 1, 2019.

"*Ad valorem* tax" means a tax which is levied in an amount determined by the value of the property being taxed.

"Advance refunding" means a bond refinancing in which the refunding bonds are issued more than 90 days before the refunding bonds are first eligible to be redeemed. A recent change in the federal tax-exempt bond laws prohibits issuing advance refunding bonds on a tax-exempt basis.

"Alternative minimum tax" means a tax (or an increased amount of the tax liability) that is due based on an alternative calculation method that might create a tax liability even if the standard calculation does not.

"Amortize" means to make periodic payments of the principal of debt.

"Appeal" or "property tax appeal" means a taxpayer challenge to the assessor's determination of the taxable value of the taxpayer's property.

"Arbitrage yield" means the interest rate percentage representing the percentage of earnings on a bond issue. The arbitrage yield on a bond issue must be calculated in accordance with highly specific and detailed federal tax rules. The arbitrage yield is used as the limit on the yield that may be earned on bond funds that are required to be yield-restricted.

"Arbitrage" means the profit that results from borrowing at one interest rate and simultaneously lending the borrowed money at a higher interest rate. Federal tax laws applicable to tax-exempt bonds strictly limit the ability of a local governmental issuer of bonds to earn or retain arbitrage profits by investing bond proceeds in investments that earn a higher rate of interest than the interest rate being paid on the bonds.

"Assessed value" means the value assigned to property by the assessing officials, on which the amount of property taxes payable by the property owner (after any exemptions or deductions) will be based.

"Assessment" means the process of determining the value of taxable property for taxing purposes.

"BAN" or "bond anticipation note" means a loan undertaken by a local governmental entity which is stated to be repayable from the issuance of bonds in the future.

"Bank-qualified bond" means that a financial institution that purchases the bond may obtain more favorable tax treatment of the interest income it receives on the bond than if the bond

were not "bank-qualified." A local governmental issuer (including related entities) generally may not designate more than $10 million of debt in a calendar year as "bank qualified," and may not designate any debt as bank-qualified in a calendar year if the issuer (including related entities) expects to issue more than $10 million in debt (including tax warrants and lease financings) in the calendar year. The designation permits financial institutions to partially avoid certain tax rules designed to lessen the tax benefits for a financial institution where the funds used to buy the bonds (the interest on which is not included in gross income of the financial institution for federal tax purposes) are traceable to funds the financial institution has received from its depositors (for which the financial institution is already receiving a tax benefit by virtue of being able to deduct the interest that it pays to its depositors as a business expense).

"Basis point" means one-hundredth of one percent.

"Blue sky memorandum" means a report setting forth the laws of selected states governing the registration requirements and exemptions for securities sold (or offered for sale) in each such state.

"Bond fund" means the fund established by a bond issuer to be used to pay principal and interest on the bonds.

"Bond rating" means a rating on a bond issue assigned by a national rating agency. Obtaining a rating on the bonds can often make it possible for an issuer to secure a lower interest rate on a bond issue.

"Bond" means a loan taken out by a local governmental unit, consisting of an instrument in which the local governmental unit agrees to repay principal and interest from specified repayment sources, in return for the sale proceeds received from the purchaser.

"Call date" means the first date on which the bond ordinance or bond resolution allows the bonds to be redeemed.

"Callable" means subject to redemption.

"Capital appreciation bond" means a bond for which interest is not payable prior to the maturity of the bond; instead, the "issued amount" of the bond is a discounted amount based on the fact that interest will continue to compound at an agreed rate rather than be paid prior to the maturity of the bond.

"Capital expenditure" means an expenditure for a capital asset, most commonly referring to an asset with a useful life of more than one year.

"Capital project" means a project that has a relatively long useful life (more than one year), such as a building or equipment.

"Capitalize" means to include as part of the cost of a capital asset.

"Capitalized interest" means interest on a bond that is treated as part of the cost of a capital asset (generally during the project construction period) and that is paid from bond proceeds.

"Certified Tech Park" means a specific business area whose purpose is to promote high technology business, which the State may designate as eligible to capture certain state sales tax revenues and local income tax revenues generated in the area for application to the costs of the development of the area.

"Circuit breaker tax credit" means the forgiveness of a portion of the property tax payer's tax liability pursuant to Indiana law. Beginning in 2007, Indiana law imposed caps on the maximum tax burden that could be placed on particular classes of taxable property, with certain property having a cap equal to 1% of the gross assessed value of the property (as in the case of a home that is the taxpayer's principal residence), 2% of gross assessed value in the case of certain other classes of property (including, for example, residential rental property), or 3% of the gross assessed value in the case of certain other classes of property (including for example, commercial property). Prior to the enactment of tax caps in Indiana, levy limited funds were entitled to receive the full amount of the maximum permitted levy amount, equal to the net assessed value available to the taxing unit times the tax rate. Similarly, rate limited funds were entitled to receive the full amount of money that the available net assessed value, multiplied by the tax rate, would produce. The tax caps added an additional limitation on the amount of money that a fund could receive, by placing a limit on the maximum percentage of gross assessed value that could be imposed on the various classes of taxable property. When tax caps are exceeded, various funds experience a reduction in the amount of money they receive. That reduction can be eliminated if enough additional assessed value is made available to the taxing unit to bring the tax rates low enough to eliminate the loss due to the impact of the tax caps (since, all other things being equal, the more assessed value available, the lower the tax rate can be).

"Claw-back provision" means a provision sometimes included in an economic development agreement whereby the local governmental entity may require the developer to pay back part or all of an incentive if the developer fails to satisfy specified commitments (such as a commitment to create a minimum number of jobs) made in the economic development agreement.

"Clearing agency" means an agency, such as the Depository Trust Company, that agrees to hold bonds for bondholders, with records of beneficial ownership in the bonds to be managed electronically rather than through the physical transfer or exchange of the bonds.

"Competitive underwriting" means the sale of bonds through an underwriter that is selected based on a bidding process.

"Conduit bonds" means bonds nominally issued by a governmental body but with a private party rather than the issuer bearing the true economic benefits and burdens of the bonds.

"Coupon bond" means a bond having coupons attached entitling whoever holds the coupons to receive interest due on the bonds. Coupon bonds were common historically, but federal tax laws now require, as a qualification for tax-exempt status, that the bonds be in "registered form" (meaning that the right to receive principal and interest is based on a formal record of ownership held by the issuer or on its behalf, rather than based on possession of the bond or the coupons).

“Credit enhancement” means the provision of additional security for a bond, such as bond insurance.

“Creed district” (or “CReD”) means an area permitted to be designated by eligible municipalities whose purpose is to promote economic development, which the State has designated pursuant to its Community Revitalization District program as eligible to capture certain state sales tax revenues and local income tax revenues generated in the area for applications to the costs of the economic development of the area.

“Current refunding” means a bond refinancing in which the refunding bonds are issued not more than 90 days before the refunding bonds are first eligible to be redeemed.

“CUSIP” means an identification code (consisting of a combination of letters and numbers) that clearing agencies such as DTC use to identify bonds and other securities. The acronym stands for Committee on Uniform Securities Identification Procedures.

“Debt limit” means a limit on the total amount of direct debt (excluding certain categories of debt such as utility revenue bonds and tax increment revenue bonds) that a local governmental entity may have outstanding at any particular time. Special taxing districts usually have their own separate statutory debt limit, usually equal to 2% of the net assessed value of the territory in the jurisdiction of the special taxing district. Financings in the form of a lease usually do not count against a local governmental entity’s debt limit.

“Debt service coverage ratio” means the ratio of (a) pledged revenues projected to be available for the repayment of existing and proposed debt to (b) the amount of total debt payments payable from the pledged source that will be due in the year during which the aggregate debt payments for the existing and proposed debt will be highest.

“Debt service” means the principal and interest due on a bond or other obligation issued by the local governmental entity.

“Debt service reserve fund” or “DSRF” is a fund set aside to fill a shortfall in case revenues projected to be available to pay principal and interest on bonds fall short.

“Defeasance” means the setting aside of funds for the remaining pay-off of a bond issue, effecting a release of the rights of bondholders in the revenue stream pledged to the bonds and the substitution of such rights with an irrevocable pledge of the account holding the funds that have been set aside.

“Design-Build Contract” means a contract pursuant to which an issuer, by following specific legal requirements, can select a company to design and build a public project on behalf of the issuer without compliance with public construction bidding laws.

“DLGF” means the Indiana Department of Local Government Finance, which regulates the finances of local government units in Indiana.

"Downgrade" means a determination by a rating agency to assign a lower rating to the bonds than originally assigned because of the rating agency's opinion that the financial strength of the issuer or the quality of the bond repayment source has deteriorated since the original rating.

"Draw bond" means a bond with respect to which the bondholder permits the issuer to make draws of bond proceeds over time rather than all at once at the time of the bond issuance, with interest not beginning to accrue on portions of the principal of the bonds until such portions have been drawn down.

"DTC" means "Depository Trust Company," the most common clearing agency used by bondholders. DTC agrees to hold bonds for bondholders, with records of beneficial ownership in the bonds to be managed electronically rather than through the physical transfer or exchange of the bonds.

"EMMA" means the "Electronic Municipal Market Access" system. The Municipal Securities Rulemaking Board ("MSRB") established the Electronic Municipal Market Access system ("EMMA") in 2008. EMMA provides on-line access at no cost to various information on municipal securities, such as market statistics, information on interest rates, official statements, trade prices, and ongoing disclosure documents. The website is located at http://emma.msrb.org/.

"Escrow fund" or "escrow account" means an account created by a bond issuer into which the issuer deposits funds held by an entity with trust duties and pledged to the repayment of bonds being refunded. By establishing an escrow fund, the issuer is usually able to effect a release of its pledge of the original bond repayment source to the bondholders of the bonds being refunded.

"Executive session" means "a meeting from which the public is excluded, except the governing body may admit those persons necessary to carry out its purpose . . .." (IC 5-14-1.5-2(f).) The authority to hold an executive session is limited to particular purposes and special notice requirements, as set forth in IC 5-14-1.5.

"Executive" means, for a city, the Mayor; and for a town, the Town Council President.

"Fiscal body" means, for a city, the Common Council; and for a town, the Town Council.

"Fiscal officer" means, for a second class city, the Controller; for a third class city, the Clerk-Treasurer; and for a town, the Clerk-Treasurer.

"G-37" means the MSRB rule prohibiting "pay to play" practices by underwriters who might hope to win municipal business from local governments by making political contributions to local officials and candidates in municipalities.

"Gateway" means Indiana's electronic system requiring various periodic filings by local government officials (usually the city or town's Clerk-Treasurer of City Controller) of financial information relating to local government revenues and expenditures and related matters. The site makes such information available for the public to access and review. The Gateway website is at https://gateway.ifionline.org/

"General obligation bond" means a bond secured by a commitment of the issuing local governmental entity to levy property taxes to pay principal and interest.

"Gross assessed value" means the assessed value of property before the application of available deductions or exemptions.

"Gross funding of escrow" means that all necessary funds to provide for the retirement of existing debt are deposited into the escrow fund upon issuance of the refunding bonds, with such funds to remain uninvested.

"Homestead" means the home owned by a taxpayer which is the taxpayer's principal residence. Second homes are not homesteads.

"Indiana State Board of Accounts" is the state agency that performs periodic audits of Indiana governmental entities. The website is at https://www.in.gov/sboa/

"Installment payment" means a scheduled payment of part of the principal of a bond.

"Insurance break even" means a report, often prepared by an underwriter on insured bond issues, establishing that insurance on a bond issue is in fact financially advantageous, when comparing the price of the insurance to the savings to the issuer in interest expected to result from having bond insurance.

"Interest during construction" means the interest payable on a bond issue while the project is being constructed. Such interest is typically permitted to be funded with the proceeds of a bond issue.

"Investment grade" means that the bond issue has earned a high enough rating to indicate that the risk of non-payment is relatively low.

"Issuer" means a local governmental entity (such as a city or town) that is undertaking a borrowing by selling bonds or other obligations.

"IURC" means the Indiana Utility Regulatory Commission, which generally has rate-setting oversight for municipal utilities subject to its jurisdiction. Municipal sewage works generally are not subject to any IURC approvals, and municipal waterworks that have "opted out" of IURC jurisdiction are also generally not subject to any IURC approvals. The IURC's website is at https://www.in.gov/iurc/. A list of withdrawn municipal waterworks utilities can be found at https://www.in.gov/iurc/files/Withdrawn%20Muni%20Water%20Alpha%202%208%2018.pdf.

"Junior debt" means debt with respect to which the claim of the bond owners on the revenue source pledged to the debt is subordinate to the claim of certain other debt payable from the same source.

"Lease financing" means a financing where, instead of issuing direct debt, a local governmental entity leases the property being financed from a lessor (such as a Redevelopment Authority or a non-profit building corporation), and makes lease payments to the lessor. The lessor issues the debt, builds the project, and then leases the project to the local governmental entity. The

lessor repays its debt from the stream of lease payments it receives. A long line of Indiana Supreme Court cases have held that the payment of lease payments generally does not constitute "debt" for purposes of debt limits.

"Legislative body" means, for a city, the Common Council, and for a town, the Town Council.

"Levy limit" means the maximum dollar amount legally permitted to be raised from property taxes for a particular fund in a particular calendar. Municipal levy limits are permitted to increase each year by the lesser of (a) 6% or (b) the average annual increase in Indiana non-farm income in the most recent six years, as established by the DLGF each year.

"Levy" means the raising of property taxes.

"Levy-limited fund" means a local government fund or school fund that has a statutorily fixed limit on the amount of property taxes that can be raised for the fund in a given year.

"Local income tax" means a tax on the income of specified taxpayers that counties are able to impose and distribute to the county unit and other local governmental units in the county.

"Lucrative office" means a governmental position that produces financial benefit to the holder of the office. Indiana's constitution prohibits an individual from holding two lucrative offices at the same time. Membership on a redevelopment commission does not generally constitute a lucrative office.

"Mandatory sinking fund redemption" means the scheduled redemption of part of the principal amount of the bonds required to occur at periodic intervals tied to the principal payment schedule of the bond issue. The amount scheduled to be redeemed must be a multiple of the minimum permitted denomination applicable to the bond issue. The outstanding bonds are treated as if the bonds are all broken down into the minimum denomination, and a random selection of such deemed minimum denomination bonds is made by the trustee or paying agent to determine the specific bonds or portions of bonds to be redeemed on the mandatory sinking fund redemption date. "Serial bonds" are sometimes collapsed into "term bonds." For example, an underwriter sometimes might request that two separate serial bonds (one in the principal amount of $200,000 maturing July 1, 2020, and the second in the principal amount of $300,000 maturing July 1, 2021) be turned into term bonds in the aggregate principal amount of $500,000 all maturing on July 1, 2021, with $200,000 in principal to be randomly selected by the issuer for redemption on July 1, 2020. This is done when the underwriter believes that the total interest cost of two serial bonds will exceed the total interest cost of one term bond with one (quasi-blended) interest rate, with mandatory sinking fund requirements.

"MSRB" means the "Municipal Securities Rulemaking Board," a federal board charged with issuing rules (subject to SEC approval) designed to protect the interests of investors and governmental issuers, regulating the activities of dealers, underwriters and municipal advisors, and to analyze and publish market information. The MSRB's website is at http://www.msrb.org/

"Negotiated underwriting" means an underwriting in which the underwriter is selected based on the issuer's preference, rather than through a competitive process.

“Net assessed value” means the assessed value of taxable property after the application of available deductions and exemptions.

“Net funding of escrow” means that the amount put into an escrow fund for the pay-off of refunded bonds is a net amount such that such deposited amount, together with fixed interest earnings on securities purchased with the funds in the escrow fund, will be sufficient to pay off the refunded bond issue.

“Neutralization” means the annual process of neutralizing the impact of reassessment or trending on the allocation of assessed value between the base assessed value and the incremental assessed value of property in a TIF district.

“Note” means a relatively short-term borrowing by a local governmental entity.

“OCRA” means the Office of Community and Rural Affairs, an Indiana State agency that provides grants to municipalities for specified purposes.

“Official Statement” or “O.S.” is a document provided by a bond issuer to potential buyers of bonds to inform them of the features of the bonds, the risks of investing in the bonds, and similar information.

“Opportunity Zone” means an area suffering economic distress that has been nominated by the State and approved by the Secretary of the U.S. Treasury for such designation. Certain kinds of investments in such a zone may be eligible for favorable federal tax treatment.

“Opting out of IURC jurisdiction” means complying with the legal requirements for removing a municipal waterworks, gas utility or electric utility from the jurisdiction of the IURC with respect to debt issuance and rate-setting.

“Original issue discount” means an amount paid by bondholders for bonds that is less than the face amount of the bonds. Where this occurs, the federal tax laws prescribe special rules on how such discount must be treated for federal tax purposes.

“Original issue premium” means an amount paid by bondholders for bonds that exceeds the face amount of the bonds. Where this occurs, the federal tax laws prescribe special rules on how such premium must be treated for federal tax purposes.

“Parity debt” means debt with respect to which the claim of the bond owners on the revenue source pledged to the debt is equal to the claim of certain other debt payable from the same source.

“Parity tests” means conditions that an issuer is required to satisfy in order to qualify proposed additional debt to have an equal claim on a shared repayment source with holders of outstanding debt secured by such source.

“Payments in Lieu of Taxes” (“PILOT”) means payments by an entity not subject to property taxes to provide funds to a taxing jurisdiction as a substitute for the taxes such entity is not required to pay.

"Petition-remonstrance process" means the process which a minimum number of petitioners, usually 500, may require the local governmental entity to undertake prior to issuing bonds (or other obligations) for a project that costs more than a specified amount (usually more than $5.17 million and up to $15.51 million, with annual increases based on assessed value growth quotient, which is 3.5% for calendar year 2020), where the bonds and that are expected to be paid at least in from property taxes. If so required, the financing may not go forward at that time unless more people sign petitions in favor of the financing than the number who sign petitions objecting to the project, during a set thirty-day period.

"Pledge" means to commit particular funds to the repayment of the local governmental entity's debt.

"P.O.S." means a "Preliminary Official statement," which is an Official Statement that is not yet finalized with information that will only be available once the bonds are sold (for example, interest rates).

"Political subdivision" means a municipal corporation or a special taxing district. It is a very broad category that includes the vast majority of local governmental entities, including redevelopment commissions.

"Property tax back-up" means a commitment by a local governmental entity to levy property taxes as a back-up source for the repayment of debt if the primary repayment source proves to be inadequate. Using a property tax back-up will usually result in a lower interest rate.

"Property tax base" means all of the taxable assessed value available to a local governmental entity for purposes of calculating property taxes.

"Public procurement laws" means laws requiring specific procedures, which may include public bidding, for the selection by a local governmental unit of a company to construct a public project, or from whom the local governmental will purchase property.

"Rate study" means a professional study, usually by a municipal advisor, to determine whether existing utility rates are sufficient to meet all of the utility's needs or whether the rates need to be increased.

"Rate-limited fund" means a fund that has a statutory limit on the rate of the tax but not on the amount of taxes that can be raised. For cities, towns and counties, the most common rate-limited funds are cumulative funds.

"Reassessment" means the statutory process for periodically re-determining the value of taxable property for property tax purposes.

"Rebate" means amounts paid to the U.S. government representing arbitrage earnings on bond proceeds.

"Referendum process" means the process which a minimum number of petitioners, usually 500, may require the local governmental entity to place on the ballot the question of whether the local governmental entity may issue bonds (or other obligations) for a project that costs more than

a specified dollar amount (usually, $15.51 million, with annual increases based on assessed value growth quotient, which is 3.5% for calendar year 2020), where the bonds are expected to be paid at least in part from property taxes. If so required, the financing may not go forward at that time unless more people vote in favor of the financing than the number who vote against it.

"Refunding bond" means a bond issued to pay off a prior bond issue, usually undertaken in order to generate interest savings because of a drop in interest rates since the issuance of the prior bonds.

"Registered bond" means a bond whose ownership is determined with reference to the ownership records of the issuer, rather than being determined on the basis of who is in actual possession of the bond.

"Reimbursement Resolution" means a resolution passed by a bond issuer that entitles it to reimburse itself from bond proceeds once the bonds are issued for project costs paid from a temporary source prior to the issuance of the bonds.

"Reserve fund" or "debt service reserve fund" means a fund established by an issuer to provide a "cushion" in case revenues pledged to the repayment of the bonds fall short of the amount needed to pay debt service.

"SEC Rule 10b-5" means the SEC rule that prohibits fraud or deceit in the sale of bonds or other securities. The Rule covers affirmative statements as well as the omission of information necessary to avoid misleading potential investors.

"Secondary market" means the market for purchasing bonds that were previously purchased by the original purchaser.

"Senior debt" means debt with respect to which the claim of the bond owners on the revenue source pledged to the debt is superior to the claim of certain other debt payable from the same source.

"Sinking Fund" means a fund established by a bond issuer for the payment of principal and interest on the bonds. It commonly contains a bond principal and interest account (from which debt service is paid) and a reserve account (from which shortfalls in the bond principal and interest account can be made up).

"SLGs" (pronounced "slugs") means U.S. government securities sometimes purchased by municipalities with funds in an escrow fund established for the pay-off of an outstanding bond issue.

"SRF" means the Indiana State Revolving Loan Fund.

"Tax abatement" means the reduction of the amount of property taxes required to be paid on taxable property for a set period of time (usually up to 10 years), in order to incentivize investment in the local governmental unit.

"Tax base" means the total taxable net assessed value in a taxing unit.

“Tax-exempt bonds” means bonds issued by (or, in some cases, on behalf of) a governmental entity whereby the holder of the bonds is not required to pay federal income tax on the interest payments it receives on the bonds. For private loans (or in the case of taxable bonds), the lender (or bondholder) is required to pay federal income taxes on the interest it receives on the loan (or bond).

“TIF District” is a tax increment financing allocation area. After a TIF District is created, taxes generated by assessed value growth in the TIF District are allocated to the Redevelopment Commission.

“TIF Revenues” are revenues generated by a TIF District.

“Trending” means the annual process for re-setting the assessed value of taxable property, generally based on recent sales of comparable properties in a particular area.

“Trust Indenture” means a document pursuant to which a financial institution with trust powers undertakes duties to protect the interests of bondholders and to administer the bond issue.

“Underwriter’s discount” means the amount an underwriter agrees to be paid at the time it buys the bonds.

“Underwriting spread” means the amount that an underwriter earns on a financing.

“Underwriting” means entering into a debt issuance sold through the services of an underwriter who makes a firm commitment to purchase the bonds at an agreed price and agrees to hold those bonds which it is unable to re-sell.

“Urban Enterprise Zone” is a geographic area designated pursuant to a State program developed to promote an increase in economic activity and investment in areas of the State deemed to be the most distressed. Nineteen (19) such areas have been designated by the State. Various tax incentives are made available for businesses that invest in the Zone.

“USDA loan” means a specific type of low interest loan made to a municipality by the U.S. Department of Agriculture for a qualified project.

“Working capital” means funds to be spent other than for capital assets.

“Yield” on a bond is the rate of return earned by an investor who buys a bond.

“Yield curve” means a graph showing how quickly or slowly interest rates are projected to rise or fall over time. The x-axis is the passage of time, and the y-axis is the projected bond interest rate. A steep yield curve indicates that the interest rates are expected to rise quickly when comparing one bond term to longer bond terms over time. Corresponding, a relatively flat yield curve indicates that interest rates are expected to rise slowly when comparing one bond term to longer bond terms over time.

“Yield restriction” means restricting the yield earned on the investment of tax-exempt bond proceeds to the arbitrage yield.

"Yield to call" means the yield on a bond calculated on the assumption that it will be financially advantageous for the issuer to call the bond on the call date rather than leave it outstanding beyond that date. For purposes of calculating the arbitrage yield, regulations require that some bonds be treated as "yield to call" bonds.

PART II.

THE ROLE OF ISSUER'S COUNSEL

CHAPTER 3. DUTIES OF ISSUER'S COUNSEL

IN GENERAL

Your city or town attorney plays a critically important role in the success of the financing. Unlike any other member of the working group, your local attorney possesses a combination of legal skills <u>and</u> familiarity with the local history, customs and personalities. Is the Town Council willing to pass an ordinance at a single meeting? Your local attorney will know if there is a history of never being willing to do so. Out-of-town professionals are highly unlikely to know this information, which can obviously have an effect on how quickly a financing can be completed. Are relations between the Mayor and the Common Council cordial or strained? Again, out-of-towners are not likely to understand the local nuances.

COLLABORATION WITH BOND COUNSEL

Throughout the financing process, bond counsel and issuer's counsel remain in close communication. They may decide that bond counsel will do first drafts of documents, subject to review by issuer's counsel (and other working group members). They may also agree that bond counsel will provide model documents to issuer's counsel, who will then produce drafts to be reviewed by bond counsel and other working group members. Bond counsel should defer to issuer's counsel's preference regarding drafting of bond documents. Prior to the bond closing (which is typically done over the phone without an actual in-person closing), issuer's counsel typically assists in the arrangements for collecting signatures on closing documents from the local officials. A focused approach by issuer's counsel can often result in savings to the municipality in issuance costs.

LOCAL GOVERNMENT PROCEDURAL LAW EXPERTISE

Providing effective service as issuer's counsel requires the attorney to have an active command of the procedural laws governing various local government meetings and official actions. Most of the matters normally addressed in the issuer's counsel's formal legal opinion relate to compliance with procedural requirements. Some of the most important subjects which issuer's counsel should master are the following.

<u>Notice of Regular Public Meetings</u>. Unless there is a specific need for a special meeting of a local government body, most of the meetings at which action is taken relating to the approval of the bond issue usually occur at regular meetings, rather than special meetings. If the schedule of regular meetings of the local government body has been properly established, then no further notice either to members of the government body or the public (or local media) is necessary. However, even for regular meetings, a copy of the agenda should be posted at the entrance to the location of the meeting prior to the meeting.

<u>Establishment of Regular Meeting Schedule</u>. Most local government bodies (including city common councils and town councils) establish a schedule of regular meetings at the beginning of each new calendar year. The local government body must promptly provide local media with a schedule of the date, time and place of regular meetings. It must also post the schedule of its

regular meetings at its principal office, or if there is no such office, at the building where the meeting is to be held.

<u>Notice of Special Meetings</u>. Issuer's counsel should ensure that any special meetings of a local body have been properly noticed.

1. **Notice to Members.** Notice of the date, time and place of a special meeting must be provided to the members of the governmental body. Any specific rules for notice to members of a special meeting that have been adopted by the governmental body should also be followed. For cities, IC 36-4-6-7(b) specifically provides that "A special meeting of the legislative body shall be held when called by the city executive or when called under the rules of the legislative body."

2. **Notice to Public (Including Media).** Unless a specific statute requires more, only an Indiana Open Door Law notice is required in advance of a special meeting. Open Door Law requirements (contained in IC 5-14-1.5) generally include providing notice (at least 48 hours prior to the meeting, not including weekends or holidays) of the date, time and place of the meeting to the local media, posting such notice (at least 48 hours prior to the meeting, not including weekends or holidays) at the principal office of the local government body or, if there is no such office, at the building where the meeting is to be held, and, if an agenda is used, posting a copy of the agenda (if any) at the entrance to the location of the meeting prior to the meeting.

<u>Compliance with Quorum Requirement</u>. For both common councils and town councils, "a majority of all the elected members of the legislative body constitutes a quorum." (IC 36-4-6-10 for cities; IC 36-5-2-9.2 for towns.)

<u>Required Number of Meetings and Required Favorable Votes to Pass Resolutions and Ordinances</u>.

1. **Adoption of resolution.** Unless the common council or town council has adopted its own special <u>additional</u> requirements or unless a specific statute requires otherwise, a common council or town council may adopt a resolution (by the favorable vote of a majority of elected members) at a single meeting.

2. **Adoption of ordinance.** Unless the common council or town council has adopted its own special <u>additional</u> requirements or unless a specific statute requires otherwise, a common council or town council generally must take two meetings (which cannot be on the same day) to adopt an ordinance (by the favorable vote of a majority of elected members). A majority vote of all elected members of the common council or town council is required to pass an ordinance. However, by complying with certain special procedures described in the next paragraph, a city or town may adopt an ordinance at a single meeting (or at two meetings on the same day).

3. **Adoption of ordinance at a single meeting.** For both common councils and town councils, adoption of an ordinance at a single meeting (or on the same day) requires

two votes, which should be reflected in the minutes of the meeting. First, a motion must be made to consider the ordinance at a single meeting, and all members of the common council or town council who are present at the meeting must vote in favor of such motion. Next, a motion must be made to adopt the ordinance, and such motion must receive the favorable vote of at least two-thirds of all elected members. (IC 36-4-6-13 for cities; IC 36-5-2-9.8 for towns.)

Notice of Public Hearing. If the action to be taken by the common council or the town council must, by statute, be preceded by a public hearing, then the following requirements generally apply.

1. **Publication and posting on newspaper website.** Most types of public hearings require publication (including posting on the newspapers' websites) one time, at least ten calendar days prior to the public hearing in two newspapers (or, in some cases, one newspaper) satisfying the requirements of IC 5-3-1. (IC 5-3-1-2(b)).

2. **No separate Open Door Law notice required when publication required.** Where notice by publication is legally required, no separate Open Door Law notice is required to be provided to the public or the media. (IC 5-14-1.5-5(e).) However, the local government body should still post the agenda (if any) at the location of the meeting prior to a meeting at which a public hearing is held.

Notice of Meeting for Receipt of Bids. Notice is generally required to be published (in the newspapers or newspaper required by IC 5-3-1) twice, at least one week apart, with the second publication to be made at least seven days before the date the bids will be received. (IC 5-3-1-2(e).)

Notice of Sale of Bonds. For obligations required to be sold pursuant to public bidding, notice is required to be published (in the newspapers or newspaper required by IC 5-3-1) twice, at least one (1) week apart, with: (1) the first publication made at least fifteen (15) days before the date of the sale; and (2) the second publication made at least three (3) days before the date of the sale. (IC 5-3-1-2(d)) Alternatively, the issuer may choose instead to comply with IC 5-1-11-2(b), which requires publication (in addition to the newspapers or newspaper required by IC 5-3-1) in a newspaper published in Indianapolis (with most issuers publishing in the *Indianapolis Court and Commercial Record*), with publication to be made twice, at least one week apart, and with the second publication made at least seven days before potential bidders are required to provide their contact information to the issuer. Under the latter method for selling bonds, the issuer is required to provide to those who have submitted their contact information (and may provide to other potential bidders in its discretion) at least 24 hours' notice of the date and time that the sale will be held. Under the first method, the issuer must lock in a specific sale date as part of the legal notice. Under the second method, the issuer has the ability to monitor the market daily and to time the sale to a day when the market is relatively favorable to the issuer, so long as 24 hours' notice of the date and time of sale of the bonds is provided to potential bidders.

Posting of Legal Notice on Municipal Website. A practice of routinely posting legal notices in a conspicuous place on the issuer's website at the same time as submitting it to the

newspaper for publication may enable a legal notice to be deemed effective if the newspaper fails to publish it timely. (IC 5-3-1-2(k).)

NOTE: the following are excellent links to websites for checking to see if legal notices were published in various Indiana newspapers:

1. Public Notice Search: http://hspa.eclipping.org/hspa/legals/
2. Website: http://indianapublicnotices.com/

ISSUER'S COUNSEL LEGAL OPINION

Issuer's counsel is invariably expected to issue a legal opinion at the bond closing. Bond counsel normally provides the requested form of opinion to issuer's counsel.

POST-ISSUANCE CHECKLIST

After the issuance of the bonds, the issuer's counsel can provide valuable assistance to the issuer by helping to monitor the financing. Among other tasks, the issuer's counsel can do the following:

Arbitrage Rebate Compliance. Inquire as to whether the issuer is having required rebate calculations performed for the issuer. In some cases, bond counsel can confirm in advance whether the bond issue is exempt from the rebate requirements. If an exemption is not available, the issuer's counsel can help make sure that a professional is engaged to do so on an ongoing basis for the issuer. Typically, rebate calculations are done annually, with actual rebate payments made (if any are required) approximately every five (5) years and upon the final retirement of the bond issue.

Continuing Disclosure. Inquire into whether the issuer is complying with its continuing disclosure obligations (if any) or has engaged a professional to ensure compliance. In addition to certain fixed filing requirements with the Electronic Municipal Marketing Access system ("EMMA"), material events must also be reported to EMMA.

Changes in Use of Bond-Financed Property. Be attentive to any changes in use of the financed project that provide private parties with any special rights to the use of the project. Maintaining the tax-exempt status of the bonds generally requires, among other requirements, that the project use and security for the bonds have only a small private component.

Financial Reporting Requirements. Assist with monitoring any financial reporting requirements agreed to by the issuer. In some cases, particularly in private placements, a bond placement agreement may require the issuer to make periodic reports to the bondholder of certain specified data.

Ordinance Covenant Requirements. Assist the issuer with monitoring compliance with covenants in the bond ordinance. For example, there may be requirements relating to the maintenance of insurance. Also, the bond ordinance typically contains requirements regarding

how revenues are to be managed by the issuer, including required deposits to various bond funds and accounts.

Management Contract Rules. Assist the issuer with compliance with management contract rules. Where the issuer engages a private manager to manage a bond-financed project, maintaining the tax-exempt status of bonds requires compliance with the so-called "management contract rules," which place limits on the term of the contract and the formula for paying the manager.

Building Corporation Matters. In a lease financing, assist the building corporation in complying with applicable corporate reporting requirements. For example, state non-profit corporation filings with the Indiana Secretary of State's office are usually required.

Trust Indenture Requirements. In financings that include a trust indenture, assist the issuer with meeting any requirements imposed on it under the trust indenture (which might include keeping minimum insurance in effect, notifying the trustee of project completion, etc.).

Transcript. Help make sure the issuer (and issuer's counsel) receives from bond counsel a copy of the full transcript of bond proceedings within a reasonable time after the bond closing.

OVERSIGHT OF BUILDING CORPORATION ORGANIZATIONAL MATTERS

Lease financings commonly include the use of a building corporation to serve as bond issuer and lessor of the financed project to the municipality, as lessee. Usually, issuer's counsel incorporates the building corporation and oversees the initial meeting of the building corporation, at which officers are elected.

SELECTION OF OTHER WORKING GROUP MEMBERS

Decisions as to whom to use for bond counsel, municipal advisor and other professionals relating to the financing belong to the local officials themselves. However, these officials often seek recommendations from issuer's counsel.

CHAPTER 4.
RELATED SERVICES OF ISSUER'S COUNSEL

IN GENERAL

Issuer's counsel on a municipal financing is often responsible for additional legal services that the project being financed requires but that do not directly relate to the bond issue. These services often include, among others, one or more of the following categories of services.

LAND ACQUISITION

Land acquisition, the acquisition of easements, and the issuance of real estate title opinions are commonly needed in connection with a project being financed with a municipal financing.

Among the Indiana statutes relating to land acquisition by municipalities are the following:

1. IC 36-1-10.5: Purchase of land or structures
2. IC 36-1-4-18: Power to acquire real property within four miles of municipal boundaries
3. IC 36-1-10: Leasing and lease purchasing structures
4. IC 36-7-14-19: Redevelopment Commission acquisition of real property
5. IC 36-7-14-25.2: Redevelopment Commission as lessee of facilities from Redevelopment Authority
6. IC 36-1-11-8: Intergovernmental property transfers
7. IC 32-24: Eminent domain

LAND DISPOSITION

Among the Indiana statutes relating to land disposition by municipalities are the following.

1. IC 36-1-11: Disposition of real or personal property
2. IC 36-7-14-22: Redevelopment Commission sale or lease of real property
3. IC 36-7-14.5: Redevelopment Authority lease to Redevelopment Commission

PUBLIC CONSTRUCTION BIDDING

Projects being paid for (or undertaken in contemplation of ultimately being paid for) from public funds are generally subject to public construction bidding and procurement laws. (IC 36-1-12.)

PUBLIC PROCUREMENT

Purchases of personal property from bond funds usually require compliance with statutory public procurement laws. (IC 5-22.)

REVIEW OF ENGINEERING OR ARCHITECTURAL CONTRACT

Public construction projects being financed with bond issues generally involve the negotiation of a contract with an architectural or engineering firm. Issuer's counsel is sometimes called on to assist the issuer in matters relating to negotiation and review of the engineering or architectural contract.

REVIEW OF PUBLIC CONSTRUCTION CONTRACT

Public construction projects being financed with bond issues generally also involve the preparation of a construction contract. Issuer's counsel is sometimes called on to assist the issuer in matters relating to the negotiation and review of the construction contract.

COMPLIANCE WITH INSURANCE REQUIREMENTS

Public financings sometimes include a covenant by the issuer to maintain (or cause others to maintain) various types of insurance, such as builder's risk insurance, liability insurance and/or owner's insurance. Issuer's counsel may be asked to assist the issuer in making sure required insurance is obtained and maintained.

REPRESENTATION OF BUILDING CORPORATION IN LEASE FINANCINGS

Many lease financings involve a non-profit building corporation that serves as the issuer of the debt and lessor of the project. The creation of such a building corporation is usually undertaken by the issuer's counsel, who then commonly represents the building corporation on an ongoing basis, including any required non-profit building corporation filings.

PART III.

OTHER MEMBERS OF THE PROFESSIONAL TEAM ON A MUNICIPAL FINANCING

CHAPTER 5.
THE FINANCING TEAM IN GENERAL

Local finance transactions vary as regards the professional team they require. Some team members are included in virtually every municipal finance transaction. Certain other team members are usually, but not always, necessary in municipal finance transactions. Certain other team members are sometimes, but not most of the time, included in local government financings. Finally, certain other potential finance team members are only occasionally needed as part of the financing team.

ESSENTIAL MEMBERS OF A MUNICIPAL FINANCING TEAM

Issuer's Counsel. Issuer's counsel is the attorney or law firm that represents the municipality and that serves as the liaison between the municipality and the other members of the professional team.

Municipal Advisor. Sometimes also referred to as the financial advisor, the municipal advisor provides the issuer with advice on all of the financial aspects of the transaction.

Bond Counsel. Bond counsel is the attorney or law firm that oversees compliance with laws governing the valid issuance of municipal debt and, if applicable, compliance with federal tax laws relating to the exclusion of interest on the debt from income tax for federal tax purposes. Occasionally, Indiana's largest issuers (for example, the State of Indiana and the City of Indianapolis) designate a second firm to serve as "co-bond counsel."

Underwriter or Bond Purchaser. Any public finance transaction will include either an underwriter or one or more bond purchasers. An underwriter is a financial company that enters into an agreement with the issuer to purchase the entire bond issue, and then sells as much of the bond issue as possible and agrees to hold any unsold debt itself until and unless it can re-sell the bonds to the public or other purchasers. In other cases, the bonds might be bought directly by one or more bond purchasers. In underwritings, there may be a group of underwriters who collaborate in underwriting the bonds (through a contract usually called an "Agreement Among Underwriters"). This group is often referred to as the "underwriter's syndicate." The leader of the syndicate is called the "senior manager," or "lead manager," or "bookrunner." In some cases, underwriters agree among themselves to serve as "co-managers." Some underwriters also involve "selling group members," which assist in selling the bonds but do not incur risk by committing in advance to purchase any part of the bonds.

The term "underwriter" is a historic term derived from the practice of bankers in London who would assume risk for a project by writing their names under information relating to risk that appeared on a Lloyd's of London sign-up sheet. This risk might relate, for example, to the possibility that a ship sailing on a voyage might be shipwrecked.

In some financings, the Indiana Finance Authority serves as the purchaser of the bonds. The Indiana Finance Authority administers a State Revolving Loan Fund program for drinking water projects and sewage works projects. Similarly, the United States Department of Agriculture

administers a program for the purchase of qualifying bonds. Only certain projects qualify for such financings, but those that do benefit from very low interest rates.

Registrar and Paying Agent. A registrar is usually a financial institution with trust powers (or sometimes the fiscal officer of the municipal issuer), that maintains the record of bond ownership, manages transfers and exchanges of bonds and authenticates the bonds. A paying agent, virtually always the same financial institution as the registrar (or the fiscal officer of the municipal issuer), is the party that receives funds from the issuer and applies the funds on behalf of the issuer to make the payments of the principal and interest on the bonds to the registered owners of the bonds, and that administers bond redemptions on behalf of the issuer. In transactions that include a trustee, the trustee normally also serves as registrar and paying agent.

FREQUENT ADDITIONAL MEMBERS OF THE FINANCE TEAM

Underwriter's Counsel. Underwriters commonly engage their own separate counsel to provide legal advice on the underwriter's compliance with the various legal requirements applicable to underwriters. In some transaction, the underwriter's counsel prepares the official statement. The costs of the underwriter's counsel services are normally paid by the issuer from proceeds of the bonds. For some financings, underwriters may feel comfortable without having their own separate counsel.

Placement Agent. Some financings do not include an underwriter but instead include a placement agent, which is a company that enters into an agreement with the issuer to use its best efforts (as opposed to making a firm commitment, as underwriters do) to find an institutional buyer or individual buyer or buyers for the bond issue. Placement agents are frequently used for bonds with features or a source or repayment that makes the bonds unsuitable to try to place with the public.

Placement Agent's Counsel. Placement agent's counsel is an attorney or law firm engaged by the placement agent to advise it on the laws and regulations that apply to placement agents. The costs of the placement agent's counsel services are normally paid by the issuer from proceeds of the bonds. For some financings, a placement agent may feel comfortable without its own counsel.

Purchaser's Counsel. In financings that are either placed by a placement agent or directly sold to one or more purchasers, the purchaser commonly engages its own separate counsel to review the transaction and the documentation for the bonds. The purchaser typically passes along its attorney's fees to the issuer to be paid from bond proceeds. Where the Indiana Finance Authority purchase the bonds through its State Revolving Loan Fund program, Indiana Finance Authority representatives and attorneys play a critical role in the financing.

Trustee. A trustee is a company with trust powers, usually a financial institution, that serves as an intermediary between the issuer and the holders of the bonds. The trustee's principal function is to protect and enforce the rights of the bondholders and to hold mortgages or security interests on behalf of the bondholders. In financings with a trustee, the trustee normally also serves as registrar and paying agent for the financing.

Rating Agency. A rating agency is a company that reviews the investment quality of a bond issue and the financial health of the issuer and assigns a bond rating to the issue. The principal rating agencies are Moody's and Standard & Poor's. The municipal advisor analyzes whether the potential savings from having a bond rating justify the cost of the rating and the additional time that may be added to the financing timetable by seeking a bond rating.

Architect or Engineer. For financings of new capital projects, the issuer typically engages an architect or engineer to design the project. This team member also advises the issuer regarding the probable cost of the project and the anticipated schedule of expenditures of the bond funds, to help ensure that the amount of the bonds is appropriate and sufficient for the particular project. The anticipated schedule of expenditures also helps the issuer to determine whether the project construction timetable will likely enable the bond issue to qualify for favorable treatment under the federal arbitrage regulations.

COMMON ADDITIONAL MEMBERS OF THE FINANCING TEAM

Bond Insurer. A bond insurer is a company that commits to make payment on the bonds if the issuer fails to do so. The most common bond insurance companies include Build America Mutual Assurance Company and Assured Guaranty Municipal Corp. In recent years, some of the previously most significant bond insurers encountered financial difficulties (leading to ratings downgrades and in some case bankruptcies). Frequently, bond insurance is coupled with a debt service reserve fund insurance policy, guaranteeing the deposit of funds into the reserve fund if reserve fund draws turn out to be needed (thereby enabling the issuer to avoid the need to fund the reserve fund with cash or securities).

Grant Writer. A grant writer is a professional who assists an issuer with applying for state or federal grants.

Escrow Trustee. In refunding bond issues, an escrow trustee (also called an "escrow agent") is a company, usually a financial institution, that holds, in trust for the owners of bonds being refunded, securities and cash provided by the issuer in an amount that is sufficient to ensure the pay-off of the refunded bonds.

Escrow Bidding Agent. In refunding issues involving the creation of an escrow fund for the benefit of the holders of the refunded bonds, an escrow bidding agent is a party that solicits bids for the provision of securities to be purchased for the escrow so that the issuer can get the most favorable possible interest rates on the securities purchased for the escrow fund.

OCCASIONAL ADDITIONAL MEMBERS OF THE FINANCING TEAM

Disclosure Counsel. In some financings, the issuer engages an attorney whose role is to ensure that the issuer provides legally sufficient disclosure to potential purchasers of the bonds.

State Lobbyist. In transactions where a change in Indiana statutes is needed, the issuer may engage a state lobbyist, who will be the liaison to members of the legislature to assist in persuading them to make the statutory change needed. This professional also may be engaged to assist a municipal issuer in connection with seeking loans or grants for the issuer from the State government.

Federal Lobbyist. A federal lobbyist is a professional who represents an issuer either with proposed changes in federal laws or regulations or in connection with seeking loans or grants for the issuer from the federal government.

Credit Enhancer. A credit enhancer provides additional security for the repayment of the bonds to make the investment more attractive in the market place. Common types of credit enhancement include letters of credit and guaranties.

Feasibility Consultant. In advance of issuing bonds, a municipal issuer sometimes engages an expert to undertake a study of the economic viability of a proposed major capital project.

Auditor. Some financings include formal audit reports as part of the official statement.

CHAPTER 6.
THE ROLE OF THE MUNICIPAL ADVISOR

IN GENERAL

Municipal advisors play a significant role in almost all municipal financings. Often, but not always, they hold CPA degrees and commonly limit their practices to financial matters for local governmental entities. Municipal advisors are required to undergo a strict licensing process including comprehensive testing. In selecting the municipal advisor for a financing, municipalities are not required to bid out the work but may select the municipal advisor of their choice. In a public financing, the issuer usually pays for the services of the municipal financing from proceeds of the financing.

FIDUCIARY DUTY

Pursuant to rules promulgated by the Municipal Securities Rulemaking Board ("MSRB"), municipal advisors assisting with a financing owe a fiduciary duty of loyalty and care to the municipality. In contrast, underwriters and placement agents generally do not have such a duty and are not required to act in the best interest of the municipality.

FEDERAL REGULATION OF MUNICIPAL ADVISORS

Municipal advisors are subject to rules promulgated by the Municipal Securities Rulemaking Board (which rules must be approved by the Securities Exchange Commission). Municipal advisors must be registered with the SEC and the MSRB. Being registered as a municipal advisor requires that the municipal advisor take and pass rigorous tests conducted by the SEC. These requirements are a fairly recent development in federal law, prior to which municipal advisors were not subject to any federal regulation. An amendment to MSRB Rule G-37, passed in 2016, effectively prohibits municipal advisors from accepting engagements from officials of municipal clients to whom the municipal advisor has provided a political contribution. Also, MSRB rules effectively prevent a municipal advisor from working "at risk" on bond issues, including refunding bond issues (unlike the common practice of bond counsel and issuer's counsel to agree to receive no payment for their services if the refunding bond issue does not close). The municipal advisor is not permitted to agree not to be compensated if a bond issue does not close.

SERVICES OF MUNICIPAL ADVISOR

Municipal advisors perform a wide range of services for their municipal clients, in the planning of a financing, during the financing process, and after the financing. Such services include, without limitation, the following.

Deciding Whether to Borrow. A municipal advisor may assist the municipality in its decision regarding whether to borrow money for a project or instead to use funds on hand, or to use a combination of debt financing and funds on hand. In advising the municipality, a municipal advisor examines factors such as the impact of depleting funds on hand that may be needed in the future, the borrowing capacity of the municipality, and current market conditions for borrowing.

Review of Sufficiency of User Rates. Municipalities normally use revenues received from utility customers as the source of repayment of bonds for municipal utility projects. As a consequence, in the planning of a utility financing, the municipal advisor reviews the sufficiency of the rates charged to customers for purposes of paying the various expenses of the utility, including operating and maintenance costs and the costs of financing new capital projects. This "rate study" helps determine whether a rate increase is advisable, and if so, the extent of the rate increase needed.

Issuance of Parity Report. Where the municipality has outstanding debt payable from the revenues of one of its utilities and wants to incur additional debt for such utility, the municipal advisor examines whether the new debt is able to be issued on a "parity basis" with the outstanding debt or must instead be issued on a "junior basis." Achieving parity status is desirable because it usually enables the issuer to obtain a lower interest rate on the new debt. "Parity status" means that the holders of the proposed new debt have an equal claim with the claim of holders of previously issued debt with respect to the pledge of net revenues of the utility to the repayment of the debt. Typical bond documents usually do not permit the issuer to issue additional debt having a parity claim on a utility's net revenues unless the issuer can demonstrate that the net revenues of the utility are projected to be more than sufficient (by a specific margin) to pay the existing debt and the proposed new debt. Commonly, the net revenues must be projected to provide a debt service coverage ratio of at least 125%, meaning that the net revenues would be sufficient to pay not just all of the debt, both existing and proposed, but, for added protection of the bond holders, would be sufficient pay at least 1.25 times the maximum annual revenues needed for debt payments. This added protection takes into account the fact that future net revenues from users of a municipality cannot be predicted in advance with certainty and may turn out to be less than originally expected. The additional coverage required for parity status provides a cushion in case actual net revenues turn out to be less than the amount projected. The municipal advisor sets forth in a document commonly called a "parity report" its finding that the projected "debt service coverage ratio" is expected to satisfy the minimum necessary for the proposed debt to have parity status with outstanding debt. If the coverage ratio cannot be met, then holders of the proposed new debt will have a claim on the shared repayment source that is "junior" to that of the holders of the outstanding debt, with holders of outstanding debt correspondingly having a claim that is "senior" to that of the holders of the proposed new debt.

Preparation of Disclosure Materials. Potential purchasers of municipal debt need to be able to assess the risks of investing in a bond issue. Most municipal financings include the production of an "official statement" that includes, among other provisions, information about the general financial condition of the municipality and risks relating to the repayment source for the debt. Often, it is the municipal advisor who prepares the official statement on behalf of the issuer. The issuer and issuer's counsel ordinarily review and comment on drafts of the official statement before it is finalized. Bond counsel typically assumes no official responsibility to review the official statement but generally provides comments as a courtesy. Prior to the production of the final official statement, it is customary for an issuer to prepare (or cause to be prepared) a "preliminary official statement." In other financings, instead of a preliminary official statement and final official statement, the issuer sometimes causes to be prepared a similar disclosure document often referred to as a "private placement memorandum."

<u>Escrow Verification Reports</u>. When an escrow fund is established to provide for the future pay-off of an outstanding bond issue, the holders of the existing debt need to know that the securities and cash being set aside in an escrow fund (including projected fixed interest earnings on any securities in the escrow fund) will be sufficient to pay off the debt through and on the date of redemption of the existing debt. To demonstrate the sufficiency of the escrow fund, the municipal advisor usually prepares a report that the escrow fund is sufficiently funded to ensure payment of interest and principal payments to and on the first permitted bond redemption date.

<u>Establishment of Bond Terms and Parameters</u>. The municipal advisor advises the issuer on how to structure the proposed debt issuance by making recommendations on various terms and parameters of the bonds. The following are some of the terms as to which the municipal advisor usually provides advice.

1. **Repayment source or sources.** Repayment sources selected as the security for the debt depend on various factors, such as the availability of certain categories of funds, state law limitations that may apply to potential sources of repayment of debt incurred for a particular type of project, debt limit considerations, and the interest rate that can likely be obtained based on a particular repayment source versus other possible sources. In some cases, state law dictates the specific type of municipal funds that may be used to repay debt. For example, in general (but with exceptions), Indiana law requires an issuer to pay debt incurred for utility improvements solely from revenues from the operation of the particular utility. Often, where the debt is to be paid from a particular revenue source, the issuer may determine to further secure the debt with a back-up commitment to levy property taxes to pay the debt (or to further secure the debt with a secondary repayment source), where state law permits such a back-up and where doing so is politically palatable.

2. **Final maturity date.** The municipal advisor makes a recommendation of the final maturity date of the bonds based on a number of different factors, including the maximum length of debt that is statutorily permitted for the particular type of bond issue; the ability to sell the debt, since potential purchasers may have their own limitations on the maximum term of debt they are able or willing to purchase; the effect that the term will have on the interest rate that can be obtained; and how much total principal and interest the issuer can afford to pay each year, based on projected available funds from the designated revenue source.

3. **Principal payment dates.** Selection of the principal payment dates is impacted by the timing of the issuer's receipt of the revenues to be used for debt repayment. (For example, property tax collections are distributed to municipalities twice each year, usually by the end of June and the end of December, and so January 1 and July 1 are common dates selected for debt payable from property taxes). If the bonds are to be issued on a parity with one or more prior bond issues, the parity tests will specify the required principal payment dates. Although principal payments are typically made annually, making principal payments on a semiannual basis (subject to any party test restrictions) may be preferable, since a semiannual schedule may allow for faster repayment of the debt than an annual principal repayment schedule,

with potential savings in interest payments. Also, market expectations may play a role in the decision.

4. **Interest payment dates.** All of the factors that impact the selection of principal payment dates also affect the selection of the interest payment dates. Interest payments are almost always due on any date on which principal payments are due, but are often made payable more frequently than principal. For example, an annual principal payment schedule combined with a semiannual interest payment schedule is a common debt service payment schedule.

5. **Redemption provisions and any required redemption premiums.** When an issuer wants to reserve the right to pay off the debt early, the market usually requires that the issuer in effect pay for that right by requiring a higher interest rate on the bonds or by requiring the payment of a premium as a condition of exercising a redemption right. This is the case because it can be expected that a decrease in interest rates during the term of the bonds may make it economically advantageous for the issuer to refinance the debt, whereas the bond purchaser would benefit in such circumstances if the debt were not refinanced.

6. **Method of bond sale.** Some types of bonds are required by Indiana law to be sold through a competitive bidding process. (Note: As of July 1, 2018, second class cities are permitted to sell any types of debt without complying with a competitive bidding process.) Other types of debt may be sold either through a competitive bidding process, the engagement of an underwriter or placement agent, or by selecting the purchaser of the issuer's choice. In situations where the issuer has a choice, the municipal advisor makes a recommendation on which sale method to use. For example, use of public bidding may result in a better interest rate. However, some types of debt are sufficiently unique or complex that a public bidding process is not likely to be a good fit. For example, tax increment revenue bonds, because the credit analysis by potential purchasers is more complicated than for many other types of bonds, are often sold through a private negotiated sale, usually either directly by the issuer or through a placement by a placement agent engaged by the issuer to find a purchaser for the bonds. Refunding bonds are also commonly sold through a private sale, which may enable the issuer to be more nimble in timing the sale to have it occur on a particular day when the market rates are relatively favorable in order to maximize savings, with the municipal advisor or underwriter able to monitor the bond market from day to day.

7. **Issuance on a taxable or tax-exempt basis.** In some cases, proposed bonds do not qualify to be issued on a tax-exempt basis. In situations where a choice is possible, the municipal advisor compares the potential interest rate benefits of tax-exempt financing with the potential advantages of not being restricted by the rules applicable to tax-exempt bonds. For example, it is sometimes the case that including "clawback" provisions in an agreement with a developer (requiring repayment by the developer of all or part of the incentive in specified events) results in an inability to issue the bonds on a tax-exempt basis, so the potential benefits of the clawback provisions must be weighed against the benefit of tax-exempt rates.

8. **Use of bond anticipation notes.** In some situations, the municipal advisor may recommend that, instead of issuing long-term debt, the issuer first issue short-term debt that is payable primarily from proceeds of the long-term debt when issued. For example, if the repayment source of the long-term debt will likely become more secure in the future rather than it is currently, the issuer may benefit from a delay in locking in the long-term rates by issuing interim debt with a shorter term and a lower interest rate. (An example is debt secured by tax increment revenues that are anticipated to be generated in the future from a project that has not yet been built but that the issuer fully expects will be.)

9. **Debt with a draw feature.** It is possible in some cases to structure debt in a way that allows the issuer to make periodic draws of bond funds rather than drawing all the money down at the bond closing, with interest not beginning to accrue on particular portions of the principal until such portions are actually drawn down. The public markets do not lend themselves to this arrangement, but for debt sold to a local bank, the inclusion of draw provisions may enable the issuer to save money in interest where not all of the money is needed immediately.

10. **Authorized denominations.** Although the traditional minimum bond denomination is $5,000 (sometimes called a "round lot"), the municipal advisor may recommend that the bonds have a minimum denomination of $100,000 or higher, since doing so (where the number of purchasers of the debt will not exceed 35, all of whom must certify that they qualify as "sophisticated investors") may enable the issuer to be exempt from preparing an official statement and continuing disclosure requirements that would otherwise be required.

11. **Advice regarding other terms.** The municipal advisor advises the issuer on various other technical terms of the debt, such as permitted interest rate multiples, good faith check deposit requirements, and the maximum underwriter bond discount that a bidder may propose as part of its bid.

Identification of Appropriate Market in Which to Sell Debt. The municipal advisor is able to advise the issuer as to who the potential buyers are for the particular bond issue. Some types of debt are not appropriate to attempt to sell in the public markets. For example, complex tax increment financings are often not suitable for sale in the public markets. In other cases, it may be advantageous for an issuer to attempt to sell the debt to a local financial institution with ties to the issuer. In still other cases, engagement by the issuer of an underwriter or placement agent may have the most advantageous results. The cost of preparing disclosure materials may make a public sale prohibitively expensive in some cases. Although the municipal advisor can help identify the appropriate pool of potential purchasers of the debt, municipal advisors are prohibited by federal law from playing a formal role in the negotiation of the sale of municipal debt to a particular purchaser.

Whether to Seek a Bond Rating. The municipal advisor reviews the advantages and disadvantages of seeking a bond rating for the bond issue. Factors that the municipal advisor considers in determining whether to recommend seeking a bond rating include the cost of a bond rating (which depends in part on the size of the bond issue but would usually in any case be upward

of 20 basis points (0.2%) of the bond principal amount), the likely interest rate savings that might result from having the bonds rated, the additional time that a bond rating may add to the timeline for completing the financing process, the risk of obtaining an unexpectedly low bond rating, and the market in which the bonds are to be sold. Some categories of bond purchasers, for example, have internal policies that limit their bond purchases to debt having a certain minimum bond rating.

Whether to Seek Bond Insurance. The municipal advisor may determine that the issuer will benefit by having the bonds insured by a bond insurance company. Factors that are considered include the cost of the bond insurance versus the savings in interest costs expected to result from insuring the bonds, whether the bonds are marketable at all on commercially reasonable terms without bond insurance, and whether the bond issue satisfies the bond insurer's minimum requirements to be eligible to purchase bond insurance from that bond insurer. The issuer (as well as the purchaser of the bonds) also needs to consider the possibility that the bond insurer may encounter financial difficulties that will make the bonds less valuable in the secondary market, as has happened in the past.

Need for Debt Service Reserve Fund. The municipal advisor advises the issuer on the necessity or desirability of funding a debt service reserve fund. In many cases, the issuance of debt on a parity basis with prior debt requires the funding of a reserve fund at a minimum specified level in order to satisfy the parity tests. For financings through the State Revolving Loan Fund, there is a standard requirement that the issuer maintain a reserve fund in an amount equal to the maximum annual debt service on the bonds and other outstanding bonds payable from the same source. In cases where the issuer is able to use a debt service reserve fund insurance policy (where, rather than funding the reserve fund with cash and securities, the issuer contracts with a bond insurer to deposit funds into the reserve fund if a draw on the reserve fund becomes necessary), the municipal advisor may advise the issuer to use that option.

Timing of Bond Sale. The municipal advisor is able to assist the issuer with respect to the timing of the issuance of bonds. If the current interest rates are relatively high but are expected to improve, the municipal advisor may advise the issuer to delay the sale of bonds. Sometimes the municipal advisor encourages the issuer to take advantage of current low interest rates that are at risk of rising. A municipal advisor also sometimes advises the issuer to issue needed debt soon enough to continue an existing tax rate currently being levied for outstanding debt that is about to be fully paid off, since doing so may not cause an increase in, but may have the effect of simply maintaining, the current burden of the debt on taxpayers. A municipal advisor may also recommend that a bond issue be delayed to a future year or done in two series issued in consecutive years in order to enable the issuer to designate the debt as "bank-qualified," since eligibility is based on the total amount of debt of the issuer in a particular calendar year.

Review of Proposed Interest Rates on Underwritten Transactions. In an underwritten financing, the municipal advisor may be able during the pricing process to compare initial public offering prices proposed by an underwriter to market rates for comparable securities on the sale date.

Eligibility of Debt for Designation as "Bank-Qualified." The municipal advisor can be expected to assist the issuer in determining whether a proposed debt issuance qualifies to be designated as "bank-qualified." The potential advantage of bank-qualified status is that the debt

is made more attractive to financial institutions, by reducing certain tax disadvantages that apply to the interest on municipal debt held by financial institutions. Eligibility for such designation generally depends on the amount of debt expected to be issued in the calendar year of issuance by the issuer and its related parties (including for such purposes tax warrants as well as other types of debt), which generally may not exceed $10 million in the calendar year in which the debt is proposed to be issued.

Review of Compliance with Constitution and Statutory Debt Limits. The municipal advisor is able to determine whether proposed debt is within any applicable Indiana state constitutional or statutory debt limits. The municipal advisor may advise the issuer to use a lease financing (which does not usually count as "debt" for debt limited purposes) rather than a direct debt financing, which may count as "debt" for debt limit purposes. The municipal advisor may also advise the issue to use lease financing simply in order to save debt limit capacity for future projects that may not be suitable for lease financing (such as where no leasable asset is being financed with the bonds).

Preparation of Tax Impact Statements in Creation or Expansion of TIF District. One of the requirements for creating or expanding a tax increment financing allocation area is the preparation by (or on behalf of) the issuer of an analysis of the impact of the proposed TIF District creation or expansion on underlying taxing units. Most commonly, Redevelopment Commissions engage a municipal advisor to prepare such report.

POST-CLOSING AND ONGOING MUNICIPAL ADVISORY SERVICES

Rebate Calculations. Municipalities are well advised to engage a professional, typically a municipal advisor, to perform legally required arbitrage rebate calculations. Compliance with rebate requirements is necessary in order to maintain the tax-exempt status of tax-exempt bonds. The complexity of the rules governing the calculations of rebate effectively makes it practically impossible for the issuer to comply with the rules without professional assistance. In some cases, bond issues are able to be structured in a way that makes them exempt from arbitrage rebate requirements, in which case no professional rebate calculation services will be necessary for such issue. The issuer's bond counsel can advise the issuer as to whether the bond issue qualifies for an exemption from arbitrage rebate requirements.

Continuing Disclosure Requirements. Municipalities are also well advised to engage the services of a professional, typically a municipal advisor, to assist the issuer in complying with ongoing municipal disclosure filings that may apply to the bond issue. Because of increased scrutiny in recent years by the Securities and Exchange Commission, municipalities also often find it necessary to engage a municipal advisor to review past compliance with the issuer's continuing disclosure obligations and, if necessary and possible, to correct any errors or omissions in filings. Federal securities law requires that the issuer include in the Official Statement a summary of any failures by the issuer, within the prior five years, to comply with its continuing disclosure commitments.

Monitoring of Covenant Compliance. The municipality can benefit from engaging a municipal advisor to assist with monitoring compliance with bond covenants relating to such

matters as annual reports that the municipality may have committed to a bondholder to provide on a periodic basis.

Monitoring of Opportunities for Savings from Refundings. Many municipal advisors keep an internal system for monitoring opportunities for savings to the issuer through refunding an outstanding bond issue, where the market has improved sufficiently for the refinancing to generate savings.

Budget Advice. Many issuers find it beneficial to engage a municipal advisor to provide ongoing budgeting advice, including long-term financial planning.

Utility Rate Studies. A municipal advisor can be helpful to issuers in monitoring the need for utility rate increases by undertaking periodic rate studies to enable the issuer to make decisions on the amount and timing of potential rate increases. The municipal advisor can advise the issuer on how the issuer's utility rates compare to those of other similar municipalities, and can help in the communication to the public of the need for a rate increase, including whether the amendment to the rate ordinance should provide for an immediate or a gradual increase in rates.

TIF Calculations, Reporting and Monitoring. It is common for a Redevelopment Commission to engage a municipal advisor to assist with various reporting requirements applicable to Redevelopment Commissions that have created tax increment financing allocation areas. Careful monitoring of annual TIF calculations made by the Auditor's office can help identify unintended errors that may result in the Redevelopment Commission's receiving less in TIF draws than the amount to which it is legally entitled. In addition, municipal advisors are able to assist with TIF projections in formulating possible incentives to developers.

CHAPTER 7.
THE ROLE OF BOND COUNSEL

HISTORICAL EMERGENCE OF BOND COUNSEL VALIDITY OPINIONS

The practice by local governments of offering incentives in order to spur economic development did not begin in our own era. In the second part of the 19th century, localities were eager to incentivize growth by offering subsidies to railroad developers. The common belief was that attracting a railroad to pass through your town was a virtual guarantee of growth and prosperity for your community. Strong public support by local constituencies for offering attractive subsidies to companies interested in bringing their towns into the railroad network was the norm. Countless local and state governmental entities issued bonds to provide such subsidies. Sometimes, the bond funds would be used to buy stock in a railroad company that would commit to expanding into the community. In other cases, the bond funds would be used to buy real property to be offered to the railroad as an incentive. Increased tax revenues would surely follow from the investment, it was assumed, and those additional revenues would provide an ample source of funds for the repayment of the debt.

The development of an extensive network of railroad lines changed the course of history for the United States. Once railroads enabled goods (including crops) to be shipped long distances, a highly rural nation became an interconnected network of thriving cities and towns with thriving industries and economies. Sizeable local public subsidies were an essential cause of the growth of railroads. However, the investment did not always prove successful. Many communities provided wildly unrealistic levels of incentives, and many others invested in undertakings that were at best speculative. There soon emerged a sizeable percentage of communities that could not repay the debt. When investors in the debt sued, many of them learned the hard way that technical defects in the issuance of the debt rendered the debt void.

One of the principal market reactions to the defaults was the emergence of a requirement by buyers of bonds that municipal debt issuances be accompanied by a validity opinion from attorneys with specific expertise in the statutory procedures for the issuance of valid municipal debt. Even though the issuer pays for the services of bond counsel, bond counsel is by necessity required to have sufficient independence to ensure the reliability of its bond counsel opinion. The risk of having one's investment ruled by a court to be void was substantially reduced by this new practice of requiring a specialized legal opinion of bond counsel.

"NATIONALLY RECOGNIZED BOND COUNSEL"

The "Bond Buyer" annually publishes a book called the "Bond Buyer's Municipal Marketplace" (and known more commonly as the "Red Book") that lists those individuals and firms that have experience serving as bond counsel on municipal financings. Although not a strict legal requirement, it is recommended that local municipalities select bond counsel from among those included in the Red Book.

FEDERAL TAX COMPONENT OF BOND COUNSEL OPINION

In 1913, the 16th Amendment to the United States Constitution authorized Congress to impose a federal income tax. The Revenue Act of 1913 was then passed, and specifically excluded the interest on state and local bonds from federal income taxation.

Concept of "Tax-Exempt" Bond. Suppose an individual takes out a loan from a bank. When the borrower repays the principal to the bank with interest, the bank must generally include the interest it receives as taxable income for federal income tax purposes. However, for most municipal debt, the bondholder (i.e., the lender to the issuer of the bonds) does not have to pay federal income tax on the interest income it receives. As a result, the bond purchasers are generally willing to accept a lower interest rate from local governments than they would require from a private borrower, since the effective return for taxable debt is reduced by the federal tax liability, which investors generally do not have to take that into account in the case of tax-exempt bonds.

To have their debt qualify for federal tax-exempt treatment, states and municipalities must comply with a wide range of technical requirements as of the date of issuance of the debt and continuing after the issuance of the debt. The principal requirements to qualify municipal bonds for tax-exempt status include the following.

Limitation on the Amount of "Private Use" and "Private Payment or Security." If a local government could issue tax-exempt debt to build a building with the intention of leasing it to a private company in return for lease payments sufficient to enable the local government to pay the debt, the local government would effectively be able to pass along its lower borrowing costs to a private entity. The policy of the federal tax laws is that the benefits of tax-exempt financing should be available only for truly governmental projects. Consistent with that policy, there are strict limitations on the extent to which a project financed with tax-exempt bonds can be privately used by parties paying the local government for (or otherwise providing security to the local government in return for) the private use. As a general rule, a governmental project that involves more than 5% private use by a party or parties securing or paying more than 5% of the debt service on the bonds will not qualify to be financed using tax-exempt debt. (Note that the federal tax-exempt bond laws do include special rules that allow private use and private payment for certain types of benefiting entities (such as tax-exempt hospitals and universities) or for certain types of projects (such as airports).

Limitation on Earning and/or Retaining Arbitrage Profits; Concept of "Arbitrage." Arbitrage earnings arise when a party borrows money at one rate (say, 4% per annum) and then invests the borrowed money at a higher rate (say, 6% per annum). The two percent profit is labelled "arbitrage." The policy behind the arbitrage provisions in the tax-exempt bond laws is that a local government benefiting from tax-exempt bond financing should not be able (in most situations) to invest bond proceeds at a rate higher than the rate of interest on the bonds; and also, that, even in those limited cases where the local government is permitted to earn arbitrage, the local government should not (with narrow exceptions) be allowed to keep the profit, but instead should be required to turn it in to the federal government (referred to as "rebating" the earnings to the federal government).

Federal Information Return. An additional requirement for tax-exempt status of bonds is that the issuer must file a federal tax return reporting the issuance of the bonds (usually on I.R.S. Form 8038-G), which must be filed not later than the fifteenth day of the second calendar month in the quarter of the year succeeding the quarter in which the bonds are issued (for example, by May 15 for bonds issued between January 1 and March 31, and by August 15 for bonds issued between April 1 and June 30). Typically, bond counsel assumes the obligation to make this filing on behalf of the issuer.

STATE TAX COMPONENT OF BOND COUNSEL OPINION

The standard Indiana bond counsel opinion also includes a statement that the interest on the bonds is also exempt from taxation for Indiana income tax purposes (except the Indiana financial institutions tax).

USE OF TIMETABLE AND CHECKLIST

Most Indiana bond counsel will, at the start of a bond financing, prepare a detailed timetable and checklist setting forth the various action items that need to be taken, and on what date, in order to satisfy legal requirements for the valid issuance of the debt. Some timetables also include statutory citations that indicate what statute governs the particular action item. So, for example, a timetable will typically indicate the dates on which public hearings or meetings will be held by local governmental bodies, dates for publications of any required legal notices, and any other entries that are useful for keeping the financing process on track.

"SHEPHERDING" OF BOND PROCEEDINGS BY BOND COUNSEL

Since most local counsel are involved in bond financings only from time to time, it is reasonable for the local counsel to expect that bond counsel will specifically request of local counsel any action items that the local counsel needs to take care in connection with the bonding process.

STANDARD BOND DOCUMENTS

The most common bond documents include the following.

Bond Ordinance or Bond Resolution. The bond ordinance (or the bond resolution, for some issuers such as a park district, without the ability to pass ordinances) is the principal document authorizing the issuance of the bonds and setting forth the general terms of the bonds. This document typically covers the following:

1. Authorization of issuance of the bonds

2. Maximum authorized principal amount of the bonds

3. Maximum interest rate on the bonds

4. Description of project being financed

5. For a refunding bond issue, description of the bond issue being refunded

6. Recitation of outstanding bonds payable from the same source of funds, if bonds are payable from a source already pledged to existing debt

7. Name of bonds

8. Denomination of bonds (i.e., minimum increments, such as $5,000)

9. Basis for calculating interest (e.g., on the basis of twelve (12) thirty (30)-day months for a three hundred sixty (360) day year)

10. Interest payment dates (usually semiannual)

11. Principal payment dates (usually annual but sometimes semiannual)

12. Designation of registrar and paying agent for bonds

13. Provisions governing transfer and exchange of bonds

14. Bond redemption provisions (or statement that bonds are not redeemable)

15. Use of Clearing Agency, if applicable

16. Form of bond (with blanks to be filled in prior to issuance)

17. Method of bond sale

18. Maximum bond discount

19. Requirements of publication of notice of intent to sell bonds, if applicable

20. Requirements for bidders

21. Deposit of funds to construction fund (or escrow agreement for refinancings)

22. Flow of funds (for example, for utility revenues, a deposit to a fund for operation and maintenance costs is typically the first bucket, followed by a deposit to a "sinking fund" used for payment of debt service, and then permitted deposits to an improvement fund)

23. Permitted investments for funds

24. Reference to the ordinance or resolution governing utility rates and charges, if applicable

25. Defeasance provisions (i.e., requirements applicable to effectively retiring the debt by depositing sufficient funds into an escrow fund pledged to the outstanding bondholders)

26. Requirements for issuing parity bonds

27. General covenants

28. Authorization of preliminary official statement, official statement and continuing disclosure agreement

29. Covenants regarding maintenance of tax exemption

30. Process for amending bond ordinance (with or without consent of bondholders)

31. Authorization of bond anticipation notes

32. Authorization of sale of bonds to State Revolving Loan Fund

33. Payments on holidays

34. If applicable, designation of bonds as "qualified tax-exempt obligations"

Rate Ordinance. In the course of undertaking a revenue bond financing, there may be a need for a rate increase. This is typically done by ordinance, following a public hearing.

Appropriation Ordinance. Some types of bond issues, especially bonds payable from *ad valorem* taxes, require an additional appropriation process. Commonly, this involves the adoption of an appropriation ordinance following a public hearing, with a filing of a report made afterward to the Department of Local Government Finance.

Resolution of Subordinate Body. It is good practice to have the applicable subordinate board, such as a board of public works and safety, take recommending action relating to a new project to be financed with bonds.

Approving Resolution of Elected Body. A recent theme that has emerged in Indiana law is that financings ought to be approved by an elected body, when a non-elected body is the principal party authorizing the bonds. Accordingly, many statutes now require such approval by the unit's fiscal or legislative body.

Legal Notices. The issuance of bonds commonly includes the publication of one or more legal notices. Some of the more typical notices include the following.

1. **Notice of Adoption and Purport.** This notice is generally required in sewage works financings where the project being financed is not being undertaken in order to comply with an IDEM order. Certain objection rights are available to the public in response to this notice.

2. **Notice of Public Hearing on Additional Appropriation.** This notice is typical in bond proceedings involving the issuance of bonds payable from *ad valorem* property taxes.

3. **Notice of Hearing on Rate Ordinance.** Utility rate increases generally require a public hearing following publication of a legal notice of the hearing (and typically also require notice of the hearing to be mailed to out-of-town customers).

4. **Notice of Public Hearing on Lease.** Official action approving a financing lease usually includes a public hearing and preceded by a published notice of such hearing.

5. **Notice of Execution of Lease.** It is a common statutory requirement for lease financings that the lessee publish notice of the execution of the lease.

6. **Notice of Determination to Issue Bonds.** This notice is required for some financings to put the public on notice that a bond issue is being proposed.

7. **Notice of Intent to Sell Bonds (or Bond Sale Notice).** This notice is used in connection with the sale of bonds being sold through competitive bidding.

8. **Preliminary Official Statement.** In financings being offered for sale to the public, this document is prepared and disseminated in advance of the sale of the bonds to provide the market with detail as to the terms of the bonds and to make potential buyers aware of the risks associated with the bonds.

9. **Final Official Statement.** After the sale of the bonds for which a Preliminary Official Statement has been prepared, the Preliminary Official Statement will be turned into a Final Official Statement by filling in blanks relating to bond terms that are not finalized until the sale of the bonds (such as the actual interest rates on the bonds).

10. **Agreed Upon Procedures ("AUP") Consents.** In financings that involve an accounting report such as an escrow verification report (demonstrating that the escrow fund has sufficient funds to pay off debt being refunded), the municipal advisor will usually require the issuer and bond counsel to agree upon the procedures to be followed in preparation of the report.

11. **Underwriter's Initial Disclosure Letters.** Federal securities laws generally prohibit an underwriter from providing advice to a municipal issuer until the underwriter has been formally engaged. As part of the formal engagement letter, the underwriter informs the municipal issuer of the scope of legal duties to which the underwriter is subject.

12. **Bond Purchase Agreement.** This document, signed by the municipal issuer and the bond purchaser (including an underwriter selected by negotiation), commits the municipal issuer to sell the bonds to the purchaser (or the underwriter) and commits the purchaser (or the underwriter) to purchase them, on a "firm offer" basis. Competitive underwritings do not customarily include a bond purchase agreement.

13. **Continuing Disclosure Agreement.** For most publically offered financings, the underwriter is required by the federal securities laws to obtain an agreement from

the obligated municipal issuer to provide certain ongoing information intended to enable the secondary market to evaluate the quality of the investment and the financial condition of the issuer.

14. **Escrow Agreement.** In a refunding issue, it is common to have an escrow agreement, under which the municipal issuer places sufficient funds with a trust agent to effect the pay-off of the bonds being refunded.

15. **Trust Indenture.** This document, common in lease financings and economic development revenue bond issues, is a contract with a trust agent that imposes on the trustee fiduciary duties to look out for the interests of the debt holders, as well as to administer the process of bond exchanges and transfers and similar functions.

16. **Financing Agreement.** This document is common in economic development revenue bond financings and contains the agreement of the municipal issuer to loan or provide the bond proceeds to the benefiting entity, and related provisions.

STANDARD CLOSING AND TRANSCRIPT DOCUMENTS

Minutes of Meetings. The transcript of proceedings generally contains copies of the official minutes of public meetings at which actions relating to the authorization and issuance of the bonds were approved.

Proofs of Publication of Notices. Where any notices have been required to be published in connection with the financing, copies of official proofs of publication are normally included in the transcript of proceedings.

Signed Resolutions and Ordinances. Copies of signed resolutions and ordinances passed as part of the bond proceedings are normally included in the transcript of proceedings.

Specimen Bond. The transcript of proceedings should include either a form of bond or a copy of one or more of the bonds.

Sophisticated Investor Letter. In some transactions, a municipal issuer can avoid federal disclosure requirements by limiting the sale of the bonds to no more than 35 purchasers who certify that they are sophisticated investors (i.e., not just a "Mom and Pop" purchaser, but a financial institution or similar knowledgeable purchaser) and setting the minimum denomination of the bonds at $100,000 or higher (an amount that usually only an institution or a sophisticated and wealthy individual could afford).

General Certificate. The issuer's general certificate contains various provisions relating to the bonds, such as an assertion that no litigation has been filed relating to the bonds; confirmation that the issuer believes that any disclosure materials were accurate, complete and not misleading; and the issuer's certification that passage of authorizing documents occurred at meetings duly called, with the approval of the requisite number of council members.

Certificate of Registrar and Paying Agent. In most financings, the municipal issuer engages a bank or trust company: (1) to keep a bond register containing the names of the legal

owners of the bonds; (2) to authenticate the bonds; and (3) to bill the issuer when payments on the bonds are due and transmit the payments to the bondholders on behalf of the municipal issuer. In this certificate, the registrar and paying agent provides evidence of its corporate powers to serve as a registrar and paying agent and the authority of its officers to authenticate the bonds and execute related documents.

Certificate of Trustee. In financings that include a trust indenture, the trustee is normally asked to attest to its trust powers and the authority of officers of the trustee to execute the trust indenture and to authenticate the bonds.

Certificate of Escrow Trustee. In financings that include an escrow agreement, the escrow trustee provides a certificate similar to a certificate of trustee.

Signature and No Litigation Certificate. A certification of the official signatures of the signers of the bonds and related documents is normally included in the transcript of proceedings.

Arbitrage and Tax Certificate. In tax-exempt financings, the issuer is required to execute a certificate relating to its expectations that the proceeds of the bonds will be invested in a manner that does not violate the limits on earning and retaining arbitrage profits on funds connected (directly or indirectly) to the financing. This certificate also typically contains other certifications relating to compliance with the restrictions that apply to tax-exempt bonds, such as limiting private use and private security to permitted levels.

Certificate of Delivery and Payment. The municipal issuer (or a registrar or trustee on its behalf) normally certifies that it has delivered the bonds to the purchaser (or to a clearing agency on its behalf, such as DTC) as part of the bond closing and that the municipal entity (or its agent) has received the bond funds.

Receipt for Bonds. The purchaser normally certifies that it has received the bonds as part of the bond closing.

IRS Form 8038-G. Filing this federal tax form is a standard requirement to qualify bonds for tax-exempt status, and a copy of it should be included in the transcript.

Parity Report. Typically prepared by the municipal advisor, this document, if applicable, provides the analysis to support the conclusion that the holders of the bonds being issued will have a co-equal claim with prior debt holders with regard to the payment source for the bonds, including compliance with the minimum debt service coverage ratio requirement for parity status.

Certificate of Municipal Advisor. This certificate sets forth various pieces of information relating to the financial aspects of the bonds, such as the arbitrage yield calculation. In this certificate, the municipal advisor, in financings with debt service reserve funds, typically certifies as to the reasonableness of the size of the reserve fund, thereby assisting the issuer in establishing its right to invest the fund at an unrestricted yield for arbitrage purposes (but subject to any rebate requirement).

Certificate of Underwriter (including compliance with Issue Price Rules). In a financing that includes an underwriter, the underwriter is required to deliver a certificate that

enables the municipal issuer to comply with the rules for calculating the yield on the bonds, which will be used to ensure compliance with various arbitrage rules requiring that bond proceeds not be invested in investments earning a higher yield than the bond yield (subject to exceptions that may permit such higher yielding investments).

Escrow Verification Report. Typically prepared by the municipal advisor, this report certifies that the amount of funds in a refunding escrow account will be sufficient to pay off the refunded bonds in full on the required payment date.

SLGs Subscription or Documentation Relating to Bidding of Escrow. The federal government runs a program of offering for sale U.S. securities, commonly referred to as SLGs (U.S. Treasury Obligations—State and Local Government Series), that an issuer is generally permitted to purchase for funding an escrow agreement. Alternatively, in some refundings, the escrow securities may be selected pursuant to a bidding process.

Additional Documents Normally Required in a State Revolving Loan ("SRF") Financing. The Indiana Finance Authority requires a number of specific documents as part of the financing.

1. **PER (Preliminary Engineering Report) Approval.** This is a letter of approval from the Indiana Finance Authority evidencing approval of the preliminary report prepared by the project engineer for the project being financed.

2. **Financial Assistance Agreement.** This document sets forth the agreement of the Indiana Finance Authority to offer assistance to a municipal issuer by providing a low interest loan subsidized by funds received by the State from the EPA.

3. **Engineer's Certificate.** This certificate, prepared by the project engineer, provides the expected schedule of expenditures of the bond proceeds and calculates the average economic life of the project being financed.

4. **Program Representative Certificate.** This document, issued by the Indiana Finance Authority, summarizes the term of the bonds and the expected source of funds to be used to purchase the bonds.

5. **Agreement with OCRA.** Many municipal financings have a grant component, with a grant for the Office of Community and Rural Affairs ("OCRA") being among the most common types of grants. In State Revolving Loan Financings, the Indiana Finance Authority likes for a copy of the grant agreement to be included in the transcript.

6. **Agreement for Services of Registrar and Paying Agent and Trust of the Sinking Fund and Construction Fund.** This is a key document in a utility financing undertaken through the State Revolving Loan Fund. It sets forth the details of required fund transfers, contains copies of relevant authorizing documents and serves as a roadmap for the administration of the financing.

BOND COUNSEL FEES

Fees of bond counsel are typically paid from the proceeds of the issuance of bonds at or after the bond closing. Bond counsel services are not required to be bid out under Indiana law.

Fixed Fee, Hourly Fee; Hourly Fee Plus Cap; Fee Not Ordinarily At Risk. Bond counsel fees for "new money" financings are typically based on either a fixed fee or an hourly arrangement (sometimes with a cap). The fees are usually paid from bond proceeds or, if the financing does not close for any reason, other available funds of the issuer.

At Risk Arrangement for Refundings. For refundings, bond counsel often is required to work "at risk," meaning that bond counsel doesn't get paid unless the market holds and the refunding bonds are issued.

CHAPTER 8.
UNDERWRITINGS AND PRIVATE PLACEMENTS

THE UNDERWRITING PROCESS

The underwriting process typically consists of the entry into an agreement by an investment banking firm to purchase the bonds of an issuer at an agreed price. In such an agreement, the underwriter sets prices for each individual maturity of the bonds at which it will initially offer to sell the bonds to the investing market. The difference between the money the underwriter receives from reselling the bonds and the amount it pays the issuer is the underwriter's profit, commonly called the "underwriting spread." Assuming that the underwriting is done on a "firm commitment" basis (as almost all underwritings are) as opposed to a "best efforts" basis, the underwriter runs the risk that it will not be able to resell the bonds to the public at the prices it anticipated. If it cannot command the initial offering price, it will be forced either to lower the price to the investors or to hold the unsold portion of the bonds in its own inventory. If the underwriter is able to sell the bonds to investors at a higher price that the initial public offering price, the underwriter's profit will be correspondingly increased. The price to be paid to the issuer by the underwriter is set forth in a contract called a "bond purchase agreement."

Sometimes, particularly for very large bond offerings, underwriters collaborate in the joint purchase of a bond offering, forming a group referred to as a "syndicate." In such case, the members of the syndicate have a separate agreement (usually called an "agreement among underwriters") setting forth how much of the bond issue each separate underwriter will purchase and attempt to re-sell. The underwriter may be selected through a public bidding process (and must be so selected in in the case of bond issues that are subject to competitive sale laws), or may be selected on a negotiated basis without public bidding (where the bonds are not legally required to be sold at public sale).

SIZE OF U.S. MUNICIPAL BOND MARKET AND MIX OF PURCHASERS

The total volume of outstanding U.S. municipal securities in a recent year (2017) was $3.85 trillion. The principal purchasers of municipal debt in 2017 were, in order of size, individuals; mutual funds; banking institutions; insurance companies; and purchasers accounting for relatively small portions of the buying market such as foreign investors, state and local governments, retirement funds, and businesses other than financial institutions.

UNDERWRITING RISK

It is not unusual for underwriters to have advance commitments or pre-orders for the purchase of the bonds at the initial public offering price. However, it is also not uncommon that the underwriter is not immediately able to sell all of the bonds at the initial public offering price. The underwriting process is called "underwriting" because the underwriter incurs risk in the transaction. The issuer is paid the full agreed price immediately upon issuance of the bonds and need not worry further about securing its needed funds.

FEDERAL REGULATION OF MUNICIPAL BOND UNDERWRITERS

Rule G-37, promulgated by the Municipal Securities Rulemaking Board (the "MSRB"), which has regulatory authority over underwriters, provides that, although underwriters do not have fiduciary duties to issuers of municipal bonds, they nonetheless are required to have fair dealings with all parties and to refrain from engaging in practices that are unfair, deceptive or dishonest. Section 15(b) of the Securities Exchange Act of 1934 requires underwriters to register as a "broker" or a "dealer." Rule G-37 also effectively prevents underwriters from making political contributions to officials (or candidates for office) of municipalities with which they do business (or would like to do business), since they are not permitted to accept engagements for a two-year period after making a political contribution to a candidate for office in such municipalities.

MSRB Rule G-23 prohibits a party from serving as both underwriter and municipal advisor at the same time on a particular financing. Under other MSRB rules, an underwriter is prohibited from providing financial advice to a municipal issuer until the underwriter is formally engaged by the issuer, or until the issuer has entered into a formal engagement with an "independent registered municipal advisor."

PRIVATE PLACEMENTS

Part of the value that an investment banking firm can offer is its network of buyers with whom it customarily deals. Some investment banks have better networks (or better networks for certain types of bonds) than others. One way in which to tap into an investment banker's specific network of contacts, when doing so would be particularly helpful because of features of the bonds being sold that make them difficult to place through an underwriting, involves engaging the investment banker to serve as a "placement agent" for the bonds. Unlike underwritings, in which the investment banker makes a firm commitment to purchase the bond issue, in private placements, the placement agent does not make a firm commitment to place the debt but instead agrees to use its "best efforts" to do so. Placement agent agreements typically provide that, for as long as the contract is in effect, the particular placement agent will have the exclusive right to try to place the debt. Additionally, such agreements usually permit either party to end the agreement at will, while providing that the placement agent is entitled to receive its commission if the bond issue is sold within an agreed limited period of time after the contract is terminated.

In a private placement, the placement agent is typically paid on a commission basis (i.e., based on an agreed percentage of the par amount of the bonds).

In connection with the private placement, the placement agent often assists the issuer with the preparation of a disclosure document called a "private placement memorandum." This document corresponds to the official statement used in underwritings.

PART IV.

MISCELLANEOUS RELATED TOPICS AND CONCEPTS RELEVANT TO MUNICIPAL FINANCE

CHAPTER 9.
CERTAIN FEDERAL TAX MATTERS

REIMBURSEMENT RESOLUTION

Federal tax law places limits on an issuer's right to make expenditures prior to the issuance of tax-exempt bonds and later issue bonds and reimburse itself from bond proceeds for the pre-bond expenditures. To fully preserve its right to do so, the issuer needs to adopt a resolution, referred to as a "reimbursement resolution," not later than sixty days after the first expenditure which the issue wants to later reimburse (with exceptions for certain "soft costs"). Accordingly, when a tax-exempt financing is in the works, the issuer should consider the adoption of a reimbursement resolution.

"TAX-EXEMPT" BONDS

When a private individual borrows money from a bank, and then repays principal and interest to the bank, the bank is required to include the interest it receives in its gross income for federal income tax purposes. When a lender loans money to a municipality in the form of purchasing the municipality's bonds and the municipality then pays the bondholder principal and interest on the bonds, the lender is usually <u>not</u> required to include the interest it receives on the bonds as gross income for federal income tax purposes. Because lenders determine the interest rate they charge in a manner that takes into account any federal income tax that has to be paid on the interest, lenders are able to offer a lower interest rate than they would offer if the income were federally taxable (where the lender's profit will be reduced by the tax liability). Not surprisingly, the federal tax laws require a municipality to comply with a number of complex rules in order to qualify its bonds for tax-exempt status (and to retain the tax-exempt status of the bonds).

ARBITRAGE

If you borrow money at a four percent interest rate, and immediately re-loan it at a six percent interest rate, the two percent profit is referred to as "arbitrage." In the context of tax-exempt bonds, federal tax laws place strict limits on the ability of a municipality to invest bond proceeds at a rate of interest higher than the yield (approximately, the blended interest rate) it is paying on the bonds. In the first instance, municipal issuers are permitted to <u>earn</u> arbitrage only in limited circumstances. Secondarily, even in circumstances where the issuer is able to <u>earn</u> arbitrage profits, the issuer will only in specific circumstances be permitted to <u>keep</u> the profit. Instead, an issuer is usually required to calculate any arbitrage profit and pay the profit to the I.R.S. at required intervals. Such payments are referred to "arbitrage rebate" payments. Failure to comply with federal arbitrage restrictions renders the bonds taxable (retroactively to their date of issuance) for federal income tax purposes.

CHAPTER 10.
ENSURING THAT THE TAX-EXEMPT STATUS OF BONDS IS NOT LOST

Municipal bond issuers need to be careful, after the issuance of the debt, not to take action that would cause bonds to lose their tax-exempt status, and not to fail to take action required to maintain the tax-exempt status of bonds. Factors to be monitored include the following:

Private Use. If the use of the financed project is being changed from the originally planned use in a way that enables private parties to have special rights in the use of the project (i.e., other than as a member of the general public), municipal officials should call bond counsel in advance to determine whether the proposed change in use will cause the bonds to become federally taxable.

Arbitrage Rebate. Has the issuer engaged professional services to help ensure that the issuer complies with federal law requirements relating to periodic arbitrage rebate calculations? Failure to comply with the complex federal arbitrage rules can result in the loss of the tax-exempt status of the bonds.

Significant Modifications of Bond Terms. Are the terms of the debt being altered in any significant way (such as modification of interest rate or the principal repayment schedule)? Some changes in the terms trigger taxability of the bonds.

CHAPTER 11.
DEBT LIMITS AND LIMIT ON BANK-QUALIFIED DEBT

The concept of debt limits is not a single concept, a fact which often causes confusion. The following are some of the contexts in which the term "debt limit" is used.

Indiana Constitutional Debt Limit. The Indiana Constitution sets forth, in Article 13, Section 1, a limit on the amount of indebtedness that a municipality may have outstanding at any given time (equal to 2% of the net assessed value of taxable property in the territory of the municipality). In practice, this debt limit most often applies to direct indebtedness ("direct" as opposed to borrowings in the form of a lease financing) payable from *ad valorem* property taxes or local income taxes. Debt that exceeds the Constitutional debt limit is void. A number of exceptions exist to the treatment of obligations as counting against the debt limit. The most common exceptions are: lease financings, utility revenue bonds, and the debt of "special taxing districts" such as park districts or redevelopment districts. The exact text of the provision is as follows.

> ***ARTICLE 13. Indebtedness. Section 1.*** *No political or municipal corporation in this State shall ever become indebted, in any manner or for any purpose to an amount, in the aggregate, exceeding two per centum on the value of the taxable property within such corporation, to be ascertained by the last assessment for State and county taxes, previous to the incurring of such indebtedness; and all bonds or obligations, in excess of such amount, given by such corporations, shall be void: Provided, That in time of war, foreign invasion, or other great public calamity, on petition of a majority of the property owners in number and value, within the limits of such corporation, the public authorities, in their discretion, may incur obligations necessary for the public protection and defense to such amount as may be requested in such petition.*

General Statutory Debt Limit. When the definition of "net assessed valuation" was altered in 1997 in a manner that would otherwise have effectively tripled the Constitutional debt limit, the Indiana General Assembly passed Indiana Code 36-1-15. Under that statute, after the normal method of calculating debt limit, the issuer is required to divide the result by three.

Statutory Debt Limits for Special Taxing Districts. The debt of "special taxing districts" such as a park district is not subject to the Constitutional debt limit. However, most statutes governing particular types of special taxing districts have their own statutory debt limit, most commonly a 2% limit (but in some cases a higher percentage).

$10 Million Limit on the Amount of Debt that can be Designated as "Bank Qualified." Obligations issued by a municipality (including its related entities such as a park district) that does not issue more than $10 million in total obligations in a calendar year are eligible to be designated by the issuer as "qualified tax-exempt obligations" (referred to commonly as "bank qualified" debt). Financial institutions that purchase tax-exempt obligations that have been designated as "qualified tax-exempt obligations" receive more favorable federal tax treatment than for obligations that are not so designated. The favorable treatment consists of the financial

institution’s ability to avoid most of the tax disadvantage normally applicable to tax-exempt debt held by a financial institution. The policy reason for the unfavorable treatment relates to not permitting “double-dipping.” Since a financial institution receives a tax deduction for interest it pays to its depositors, the I.R.S. does not believe that the full benefit of tax-exempt status should be available with respect to the interest a financial institution receives on tax-exempt obligations that are directly or indirectly traceable to money derived from depositors.

CHAPTER 12.
FEDERAL MUNICIPAL DISCLOSURE REQUIREMENTS

Scope of Municipal Securities Market. The municipal securities market consists of approximately one million separate outstanding bond issues totaling a principal amount of approximately $3.7 trillion.

History of Federal Regulation of Municipal Securities. In the early 1930s, Congress held hearings on accusations of corporate securities fraud. Congress enacted the first federal legislation regulating securities in 1933, known as the Securities Act of 1933. Under the Securities Act of 1933, corporate issuers of securities were subjected to strict registration requirements. Issuers of municipal securities were not subjected to such regulation, since municipal securities were not viewed as an area that needed strict regulation. There has, historically, been no evidence of significant misconduct by municipal issuers. As an empirical fact, general obligation bonds issued by municipalities almost never default. It is also the case that revenue bonds issued by municipalities for essential services (e.g., sewer and water) almost never default. "Conduit bonds," where municipal bonds are issued solely for the benefit of non-governmental borrowers which bear the responsibility (rather than the municipality) for repayment of the bonds, are far more likely to default than general obligation or essential services revenue bonds, with defaults occurring most frequently in the areas of nursing homes and health care projects.

Congress passed the Securities Exchange Act of 1934 the next year, creating the Securities and Exchange Commission and giving it broad power over securities regulation. Section 17(a) of the Securities Act of 1933 and Rule 10b-5 promulgated by the Securities and Exchange Commission pursuant to Section 10 of the Securities Exchange Act of 1934 imposed "anti-fraud" requirements on all securities, including municipal securities. These anti-fraud rules gave rise to the regular use of an "Official Statement" to provide relevant information to prospective investors. This regulatory scheme continued for several decades: registration of municipal securities was not required, but anti-fraud rules did apply.

The Indiana Uniform Securities Act, at Indiana Code 23-19-5-1 also contains anti-fraud provisions, as follows:

> "It is unlawful for a person, in connection with the offer, sale, or purchase of a security, directly or indirectly: (1) to employ a device, scheme, or artifice to defraud; (2) to make an untrue statement of a material fact or to omit to state a material fact necessary in order to make the statement made, in the light of the circumstances under which they were made, not misleading; or (3) to engage in an act, practice, or course of business that operates or would operate as a fraud or deceit upon another person."

Events that Led to Stricter Municipal Securities Regulation. In 1983, the Washington Public Power Supply System (nicknamed "WHOOPS") issued bonds to finance five nuclear power plants. The plants ended up costing four times the original estimate, at the same time that demand

for nuclear energy began to decline. WPPS defaulted on payments of $5.45 billion of bonds, and bondholders were able to recover only 40% of their investment.

At the same time, the mix of purchasers of bonds shifted away from financial institutions and more toward individuals and trusts (now accounting for the purchase of about 50% of all municipal debt).

Municipal Disclosure Requirement under Rule 15c2-12. Rule 15c2-12 of the Securities Exchange Act of 1934 contains two categories of rules: (1) rules relating to disclosure required at the time the bonds are issued; and (2) rules that require an issuer to provide ongoing disclosure relating to the bonds.

1. **Principal disclosure rules applicable at the time the bonds are issued (first effective on January 1, 1990).** The principal rules applicable in connection with the proposed issuance of bonds include the following.

   (a) Bonds having a principal amount of at least $1,000,000 require the preparation of an Official Statement describing certain terms of the bonds and the risks of the bonds, as well as containing general information about the issuer.

   (b) The principal exception to this general rule is that the requirement that an Official Statement be prepared does not apply to bonds that are: (1) issued in denominations of at least $100,000; and (2) sold to no more than thirty-five persons or entities each of whom the underwriter reasonably believes: (i) 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 is not purchasing the bonds for more than one account or with a view to distributing the securities.

2. **Rule requiring disclosure on an ongoing basis after the bonds are issued (first effective generally on July 3, 1995).** For bonds for which an official statement is required, the issuer is required to comply with ongoing disclosure requirements to be set forth in a Continuing Disclosure Undertaking Agreement. Such requirements generally include the following (with compliance to be in the form of postings of the required information on the Electronic Municipal Market Access system ("EMMA") website:

   (a) The provision of **annual financial and operating date,** consisting of "[a]nnual 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) The provisions of **audits**. If not submitted as part of the annual financial information, then when and if available, the issuer must file (with EMMA) audited financial statements for each "obligated person" (usually including the bond issuer).

(c) The provision of **notices of specified events** that a potential purchaser in the secondary market would want to know about (for example, principal and interest payment delinquencies, rating changes, and similar material information).

Electronic Municipal Market Access system ("EMMA"). The Municipal Securities Rulemaking Board ("MSRB") established the Electronic Municipal Market Access system ("EMMA") in 2008. The SEC then amended Rule 15c2-12 to make EMMA the sole repository for continuing disclosure filings. The website is located at http://emma.msrb.org/.

CHAPTER 13.
PRINCIPAL LOCAL GOVERNMENT REVENUE SOURCES

In General. As a theoretical matter, local revenue sources can be generally divided into three broad categories: (a) property taxes; (b) income taxes; and (c) sales taxes. States vary in their emphasis on one or more of these categories of revenues. In a recent year (2017), the states with the lowest local property taxes (based on the effective tax rate applicable to owner-occupied homes) were: Hawaii (lowest at 0.28%, but note the high home prices in Hawaii); Alabama (0.43%); and Louisiana (0.51%). States with the highest property taxes are: New Jersey (highest at 2.38%); Illinois (2.32%); and New Hampshire (2.15%). (Indiana ranked 28th highest at 0.86%.) Of all revenue sources, property taxes are the most stable. Employment ebbs and flows and income taxes vary as a result; consumers at times tighten their belts, and sales tax revenues suffer; but property taxes are not as vulnerable to economic conditions.

Income taxes are more stable and predictable than sales taxes but not as stable as property taxes. Seven states have no income tax (as of 2017). These include Florida, Texas, Washington, Nevada, Wyoming, South Dakota and Alaska. Based on the highest marginal individual tax rate, the states with the highest income tax in 2018 were California (at 13.3%) and Hawaii (11.0%). Of the forty-three states that have an income tax, only three have a lower state income tax rate than Indiana (at 3.23%). Indiana's imposition of tax caps, combined with the increase in the aggregate permitted local income tax rate, represents a *de facto* shift away from property taxes and toward income taxes as a source of local government revenues.

Sales taxes are the most unpredictable and volatile of the three major tax categories. Only twelve states do not permit sales taxation at the local level (including, along with Indiana, Connecticut, Delaware, Kentucky, Maine, Maryland, Massachusetts, Michigan, Montana, New Hampshire, Oregon and Rhode Island). At the state level (as of 2017), sales taxation is highest in California (at 7.25%), with Indiana (at 7.0%) tied for second place with Mississippi, Rhode Island and Tennessee.

***Ad valorem* Property Taxes.** Indiana municipalities are limited in the amount of property taxes they can raise by both the tax caps and by the maximum levy law (which generally limits the amount of annual increases for "levy limited" funds to the lower of 6% or the average state-wide growth of non-farm personal income for the prior six years (which, for pay 2020, is 3.5%). Municipalities also have the statutory authority to establish cumulative capital funds (subject to maximum permitted statutory rates) to raise property tax revenues for permitted purposes. These taxes count against the tax caps but generally do not count against a municipality's maximum levy. General obligation bonds (payable from *ad valorem* property taxes) count against a municipality's tax caps but not against the maximum levy, often making it possible, subject to debt limit restrictions, for municipalities to raise funds for capital projects through the issuance of general obligation bonds.

Local Income Tax Revenues. The Indiana General Assembly recently enacted legislation (IC 6-3.6, effective January 1, 2017) to streamline and unify the previously separate local income taxes (known as the County Adjusted Gross Income Tax ("CAGIT"), the County Option Income Tax ("COIT"), and the County Economic Development Income Tax ("CEDIT")). As part of the

unification of the local income taxes, the Indiana General Assembly significantly increased the permissible maximum local income tax rate over what the maximum combined rate had been prior to the enactment of IC 6-3.6. In some counties, only the County Council has the ability to increase the local income tax rate; in other counties, the "local income tax council" (consisting of the fiscal bodies of the cities, towns and county unit, which are allocated a share of a total of 100 votes usually based on relative tax collections, and with a majority of votes required to increase the local income tax rate) is the governing body for such purpose.

Other Local Taxes. Other local taxes include the following:

1. **Food and beverage taxes.** These taxes must be specifically authorized for a particular county by state law, and funds generated are usually required to be spent for a particular purpose.

2. **Innkeeper's taxes.** Most Indiana counties have an Innkeeper's Tax. All Indiana counties have the authority to impose it.

3. **Motor vehicle excise surtax and wheel tax.** Revenues generated are required to be used for roads and streets.

Tax Increment (TIF) Revenues. Tax increment revenues provide a critical source of revenues for purposes of financing economic development and redevelopment activities.

Utility-Related Revenues. Most municipalities operate one or more utilities. Such utilities may include sewage works, waterworks, electric utilities, gas utilities and stormwater systems. User rates must be nondiscriminatory, just and reasonable.

Miscellaneous Other Revenues. These may include user fees, license and permit fees, and revenues from fines and forfeitures. Examples include the following:

1. Trash collection fees

2. Franchise fees (e.g., cable TV)

3. EMS fees

4. Fire contracts

5. Police and fire reports

6. Court docket fees

7. Parks and recreation

    (a) Pool admission fees

    (b) Green fees

    (c) Shelter rental fees

(d) Concession rentals

(e) Program fees

(f) Park rental charges

8. Parking fees and parking meter receipts

9. Community building rental

10. Other rental fees

11. Other charges for permits or services, including the following examples:

(a) Street cut permits

(b) Dog licenses

(c) Building permits

(d) Other license and permit fees

(e) Fines and forfeitures

(f) Special police patrol fees

(g) Payments for special police services at large events

(h) Fingerprint fees

(i) Accident report fees

(j) Bus fares

(k) Business licensing fees

(l) Filing fees for petitions and hearings by government boards

(m) Fees for release of towed vehicles

(n) Fees for use of credit and debit cards

(o) Fees for copies

State Grants and Loans. Local government units should stay up to date on available grants, loans and subsidies that may be available from the State of Indiana for various purposes.

Federal Funds. Local government units should also stay up to date on federal grant opportunities. In addition, local officials should consider engaging a lobbyist to monitor opportunities. Millions of dollars can sometimes be accessed.

Miscellaneous Other Municipal Funding Sources.

1. **Interest earnings.** Diligent cash management practices can be very beneficial to municipalities.

2. **Savings from bond refinancings.** Municipalities may be sitting on opportunities to reduce interest costs, and in some cases, generate additional funds, without even knowing it. Regular monitoring of refinancing opportunities is important.

3. **Funds from interlocal agreements.** Neighboring or overlapping jurisdictions may be willing to share in the costs of a particular project.

4. **Payments by tax abatement beneficiaries.** In certain circumstances, for property tax abatements first granted after July 1, 2004, a company and a local government that grants the company a tax abatement may agree to direct a portion of the abatement to which the company would otherwise be entitled, to a public or nonprofit entity established to promote economic development in the applicable unit. To determine the annual amount of such payment by the company, the local unit establishes a percentage up to 15%, which is multiplied by the amount of abated taxes (provided that the payment amount may not exceed $100,000 per year).

5. **Private contributions.** Private generosity is at times found to be more forthcoming than local government units might imagine. Corporations are sometimes willing to make contributions toward the cost of a local government's capital project.

6. **Proceeds from the sale or lease of property.** For example, some municipalities have significantly improved their financial strength by selling a public utility to a private utility company.

CHAPTER 14.
COMMON MUNICIPAL FINANCING STRUCTURES

General Obligation Bonds.

1. **General Considerations.** General obligation bonds (sometimes called "G.O. bonds") are bonds that are payable from *ad valorem* property taxes levied by the issuing governmental unit. Such bonds are commonly described as being secured by the "full faith and credit" of the issuer, but as a practical matter, this feature simply means that the issuer will, if necessary, raise property tax revenues to pay the bonds. Generally, the property tax is regarded by bond buyers as the most secure source of repayment for municipal bonds. Defaults in the repayment of general obligation bonds are essentially unheard of. Accordingly, general obligation bonds typically result in the lowest possible interest cost to the issuer. In contrast, bonds payable from income taxes or revenues are commonly regarded in the market as riskier than general obligation bonds, usually resulting in higher interest rate for the issuer than general obligation bonds. Unlike private financings, general obligation bonds issued by local governmental entities do not involve the granting of a mortgage or other security interest in the property being financed. The interest rate on general obligation bonds is a fixed rate rather than a floating or variable rate, thereby permitting the local government entity to avoid the risks associated with the ups and downs of the credit markets. The interest rate on general obligations bonds is usually required to be set based on a public bidding process (except, after July 1, 2018, for second class cities).

   In the case of general obligation bonds, the issuer imposes a tax to repay the bonds, collecting the property taxes in two semiannual installments at the same time as other property taxes are collected. Typically, interest on general obligation bonds is payable semiannually and principal is payable annually, or, in some cases, semiannually. The bond payments are made by the "paying agent" for the bonds, which may be the issuer's fiscal officer (e.g., the clerk-treasurer or city controller) or, in most cases, a financial institution selected by the issuer to help the issuer ensure that that the issuer makes its bond payments on a timely basis.

   Prior to the enactment of property tax caps in Indiana, general obligation bonds were commonly described as being payable from unlimited *ad valorem* taxes of the issuing unit (the term "*ad valorem*" referring to the feature that the taxes are tied to the value of the property being taxed). Because of the tax caps, the term "unlimited" is, technically, not an accurate description of the unit's taxing power. Indiana law lessens the impact of the property tax caps by requiring issuers to apply all tax revenues (including even general fund revenues, if such were ever determined to be necessary), to the payment of general obligation bonds before applying such revenues for other purposes.

   Cities, towns, counties (with certain exceptions for financing road improvements) and townships all have the authority to issue general obligation bonds for capital

projects owned by the issuing unit. However, as a general matter, Indiana law requires that utility improvements be financed with bonds payable solely from revenues of the particular utility rather than from general obligation bonds.

2. **Debt Limit Considerations.** The amount of general obligation bonds that an issuer may issue is limited by the debt limit set forth in the Indiana Constitution and a corresponding statutory limit set forth in the Indiana Code at IC 36-1-15. Generally, an issuer may not issue general obligations bonds if doing so would cause the amount of debt that an issuer has outstanding on the date of the proposed issue to exceed two (2%) of the net assessed valuation of property in the territory of the issuing unit as of the most recent final assessment date, divided by three.

   The issuance of general obligation bonds is further conditioned on compliance with state law procedures that become increasingly cumbersome as the amount of the proposed financing increases. The process for issuing general obligation bonds, for some financings, requires a referendum process; in other cases, a petition-remonstrance process is required. For relatively smaller issues, neither process is required.

   It is not uncommon for a governmental unit to issue bonds that are formally backed by the unit's taxing power, with the governmental unit having the actual intention to use some other source of revenues to offset the need for raising property taxes to pay the bonds. Because the issuer will be required to levy property taxes to pay the bonds if that becomes necessary, the bond purchaser will regard the bonds as general obligation bonds for purposes of setting the interest rate, and will make available to the issuer a relatively lower interest rate, at the same time that the issuer avoids levying taxes by setting aside other available revenues sufficiently in advance of the time when the issuer would have to add the levy to its budget.

   Taxes imposed to pay general obligation bonds are subject to Indiana's property tax caps. However, such taxes are classified as outside the issuer's levy limit.

3. **Preliminary Procedures for Issuing Bonds to be Paid From Property Taxes.** The procedures required for the issuance by a local government unit of bonds or lease obligations to be paid from property taxes is a very fact-sensitive inquiry. The following rules apply.

Concept of "Controlled Project." If a project is not a "controlled project," then neither the referendum process not the petition-remonstrance process will apply. Instead, a simpler set of procedures will apply.

The following types of "projects" do not meet the definition of a "controlled project:"

1. A project for which the issuer reasonably expects to pay debt service or lease rentals from funds other than property taxes (with tax increment revenues not treated as property taxes for this purpose), even if the issuer has pledged property taxes as a back up to the principal debt repayment source in the event such other pledged source turns out to be insufficient.

2. A project that will not cost the issuer more than $1 million.

3. A project that will not cost the issuer more than either of the following: (a) $5.17 million; or (b) 1% of gross assessed value of the issuer.

4. A project that is being refinanced for the purpose of providing gross or net present value savings to taxpayers.

5. A project that is required by a court order holding that a federal law mandates the project.

6. A project that is in response to a natural disaster, an accident, or an emergency in the issuing unit that makes a building or facility unavailable for its intended use, and is approved by the County Council in which the unit is located.

7. Certain other specified categories of projects involving prior approvals of the Department of Local Government Finance (or its predecessor).

Bonds or Leases Subject to Referendum Process. Bonds or leases for a municipal project are (if the requisite number of petitioners so demand) subject to the referendum process (as described below) if the project meets the definition of a "controlled project," and the project will cost more than $1 million and more than either of the following: (a) $15.51 million dollars; or (b) 1% of the gross assessed value of the issuer.

Bonds or Leases Subject to Petition – Remonstrance Process. Controlled projects of municipalities that are not large enough to be subject to the referendum process are (if the requisite number of petitioners so demand) still subject to the petition-remonstrance process.

Special Taxing District Bonds.

1. **In General.** Indiana law authorizes the creation of districts known as "special taxing districts" for various specified purposes, such as park districts, redevelopment districts, and sanitary districts. As a theoretical matter, such districts are viewed as a case of taxpayers joining together to tax themselves for a specific purpose that provides special benefits to the district and its taxpayers. Bonds issued by a special taxing district are payable from *ad valorem* taxes (sometimes called a "special benefits tax") levied on all taxable property in the special taxing district.

2. **Separate Debt Limit.** Debt issued by a special taxing district does not count against the debt limit of the unit that creates the district, but most statutes authorizing the creation of a special taxing district establish a separate statutory debt limit for debt issued by the district.

3. **Applicability of Petition-Remonstrance and Referendum Laws.** Whether bonds of a special taxing district are subject to the petition-remonstrance or referendum laws is subject to the same analysis as applies to general obligation bonds.

Lease Financing.

1. **Structure of a Lease Financing.** In a lease financing, rather than issue debt directly, the local governmental unit enters into a lease, most typically with a governmental lessor such as a Redevelopment Authority, or a non-profit corporation. The lessor entity serves as the issuer of the bonds and is the nominal owner of the project being financed, and the local government lessee agrees to make lease payments sufficient to enable the lessor to make payments on the lessor's bonds.

2. **Debt Limit.** The most common reason for a governmental unit to structure a financing in the form of a lease is that obligations in the form of a lease do not generally count against the local government lessee's debt limit. In a long line of cases, the Indiana Supreme Court has ruled that lease payments have the character of "current expenses" rather than constitution debt for purposes of the Indiana Constitutional limit on indebtedness.

3. **Applicability of Petition-Remonstrance and Referendum Laws.** Whether a lease financing is subject to the petition-remonstrance or referendum laws is subject to the same analysis as applies to general obligation bonds.

4. **Sale of Lease Revenue Bonds.** Bonds issued by a lessor entity generally may be solid either at public sale or by private negotiation.

Revenue Bonds.

1. **In General.** Indiana law contemplates that certain types of projects, such as waterworks or sewage works improvements, ought to be self-financed, and therefore requires (with certain exceptions) that bonds issued by a governmental unit to finance such improvements should be payable solely from revenues of the facility. However, because revenue bonds lack the backing of the governmental unit's taxing power, they generally bear a relatively higher interest rate than bonds backed by property taxes. Revenue bonds generally must be sold through a public bidding process except, after July 1, 2018, for bonds of a second class city. Projects financed by revenues from the facility being financed generally do not meet the definition of a "controlled project" and therefore are generally not subject to a petition-remonstrance or a referendum process.

2. **Debt Service Coverage Ratio.** Purchasers of revenue bonds normally require that the amount of annual net revenues projected to be generated from the facility to which the financing relates must be more than enough to cover the annual debt payments on the proposed debt. For example, a minimum "debt service coverage ratio" of 125% (i.e., projected annual revenues are at least 125% of maximum annual debt payments) is a common requirement demanded by the municipal market place for utility revenue bonds. Purchasers also typically require that any future debt that will be payable from the revenue stream supporting the bonds be limited to a subordinate claim to the claim of their bonds on the revenue stream,

and may not share an equal claim, unless certain tests (called "parity tests") are met at the time the future bonds are issued, consisting primarily of a required demonstration that the debt service coverage ratio (i.e., a comparison of annual projected net revenues to the maximum annual principal and interest requirements of the existing debt combined with the proposed additional debt) meets a certain required minimum, such as 125% or 150%.

3. **Debt Limit Considerations.** Under well-established Indiana Supreme Court case law, bonds issued to finance a project that are payable from revenues of the project do not count against the Indiana Constitutional or state statutory debt limit.

Financing of Public Works Projects Costing Not More than $2 Million. Indiana law (at Indiana Code 36-9-41) provides a somewhat streamlined set of procedures applicable to the financing of "public works" projects that will cost the local governmental entity $2 million or less, with the debt to be repaid from the levy of property taxes. The term "public works" is defined as a project for the construction of any public building, highway, street, alley, bridge, sewer, drain, or any other public facility that is paid for out of public funds.

Such a financing is subject to most of the requirements applicable to general obligation bonds, including debt limitations and the requirement to provide publication of notice of the determination to issue the debt, but the issuer is not required to sell the debt at public sale but may instead sell the debt privately to an Indiana financial institution. However, the term of the debt may not exceed 10 years. In addition, a minimum of at least 10 taxpayers are provided the right to file a petition within 30 days following the publication of the notice of determination to issue the debt and thereby force a hearing before the Department of Local Government Finance.

Tax Revenue Notes. Indiana law grants to cities (IC 36-4-6-20(a)), including Indianapolis (IC 36-3-4-22(b)), as well as to counties (IC 36-2-6-18(b)) and towns (36-5-2-11(d)) the authority to issue notes in an amount not exceeding 5% of the unit's total tax levy in the current year (not including amounts levied to pay bond and lease debt). The notes must have a term of not more than five years and are payable from the unit's tax revenues over the term of the notes. The proceeds of the notes may be used for the exercise of the powers of the issuing unit. Most of the procedures applicable to the issuance of general obligation bonds do not apply to the issuance of tax revenue notes. However, the tax levy to repay the notes counts against the unit's levy limit, and the notes also count against the unit's debt limit. Tax revenues notes are also generally required to be sold by public sale.

Economic Development Revenue Bonds. Indiana law (at IC 36-7-11.9 and IC 36-7-12) authorizes cities, towns and counties to issue bonds for economic development facilities and to loan, or grant, the proceeds of the bonds to a private developer. The facilities that may be financed includes real and personal property improvements, but facilities for the following are expressly disallowed: (1) private or commercial golf courses; (2) country clubs; (3) massage parlors; (4) tennis clubs; (5) skating facilities (including roller skating, skateboarding, or ice skating); (6) racquet sports facility (including any handball or racquetball court); (7) hot tub facility; (8) suntan facility; (9) racetrack; (10) airplane; (11) skybox or other private luxury box; (12) health club; (13) any facility primarily used for gambling; and (14) any store the principal business of which is the sale of alcoholic beverages for consumption off premises.

Prior to the issuance of economic development bonds, the unit's Economic Development Commission must hold a public hearing on the project (following publication of legal notice of the hearing at least ten days in advance), and must consider the impact of the proposed facilities on competing facilities in the unit. The Economic Development Commission must then pass a resolution approving the proposed financing.

Following the approval of the Economic Development Commission, the unit's fiscal body must then adopt an ordinance authorizing the issuance of the bonds and the form of the financing documents, typically including a trust indenture and a loan agreement or financing agreement. The bonds may be sold at private sale. The construction and acquisition of the facilities are exempt from the Indiana public construction bidding and procurement laws.

Economic development bonds may not be made payable from taxes levied by the governmental unit. Commonly, economic development bonds are issued purely as "conduit bonds," whereby the local governmental unit assumes no responsibility for repayment of the bonds other than from payments made to the issuer from the developer pursuant to a promissory note from the developer to the issuer to secure the issuer's loan of the bond proceeds to the developer. Having the unit serve as a "conduit issuer" can, for certain types of projects, such as new manufacturing facilities that satisfy the numerous requirements of federal law, enable the developer to obtain the benefit of tax-exempt interest rates.

In other cases (including financings to provide a developer incentive), the issuer will grant the bond proceeds to the developer to be applied to the cost of qualified facilities, and secure the bonds from a pledge of available (non-property tax) revenues of the unit (such as local income tax revenues) or, in some cases, from a pledge of tax increment revenues from the unit's Redevelopment Commission.

CHAPTER 15.
WHEN "PRIVATE BANK LOAN" IS RECOMMENDED INSTEAD OF BONDS

Unlike private entities, local governmental entities must be able to point to specific statutory authority to borrow money through issuing obligations. To protect the public, Indiana law imposes procedural requirements for the issuance of any kind of municipal debt, which requirements vary, depending on the features of the loan and the repayment source. For example, the issuance of municipal debt may be subject to public hearing requirements, referendum requirements or petition-remonstrance requirements. There may be a statutory right given to the public to object to the issuance of the debt. There may also be a requirement that the debt be sold through a competitive public sale. All required statutory procedures must be followed for the local government's debt to be valid and enforceable.

There is sometimes a local financial institution that stands ready to make what amounts to a private loan to a municipality without the municipality's compliance with legal requirements, but the municipality must be cautioned to resist the temptation.

CHAPTER 16.
VALUE OF REDEVELOPMENT COMMISSION AND TIF PROGRAM

Those cities and towns that have not undertaken a TIF program could benefit substantially by doing so. Many communities find TIF to be an extremely valuable tool in competing for investment and job creation by companies and developers. Those communities that do not have TIF programs can find themselves at a decided disadvantage in competing for investment and job creation. It is usually possible to create a TIF District for less than $10,000 in professional expenses. The following chart showing 2015 TIF revenues of some smaller cities and towns in Indiana demonstrates how valuable a TIF program can be, even for smaller municipalities.

SAMPLE 2015 TIF RECEIPTS

Municipality	2010 Population	2015 TIF Revenues
Winona Lake (Kosciusko Co.)	4908	$127,196
Cicero (Hamilton Co.)	4812	$204,046
Bremen (Marshall Co.)	4588	$840,668
Berne (Adams Co.)	3959	$786,211
Hebron (Porter Co.)	3724	$84,476
Whitestown (Boone Co.)	2867	$2,027,336
Sheridan (Hamilton Co.)	2665	$82,521
Avilla (Noble Co.)	2401	$406,825
Albion (Noble Co.)	2349	$492,874
Orleans (Orange Co.)	2147	$21,564
Montpelier (Blackford Co.)	1805	$25,067
Hamilton (Steuben Co.)	1532	$36,815
Remington (Jasper Co.)	1185	$507,432
Shipshewana (LaGrange Co.)	658	$469,606

CHAPTER 17.
EFFECT OF CIRCUIT BREAKER TAX CREDITS ("TAX CAPS") ON THE AMOUNT OF MONEY THAT CAN BE RAISED FOR VARIOUS LOCAL FUNDS

Beginning in 2007, Indiana law imposed caps on the maximum tax burden that could be placed on particular classes of taxable property, with certain property having a cap equal to 1% of the gross assessed value of the property (as in the case of a home where the taxpayer lives), 2% of gross assessed value in the case of certain other classes of property (including, for example, residential rental property), or 3% of the gross assessed value in the case of certain other classes of property (including for example, commercial property). Prior to the enactment of tax caps in Indiana, levy limited funds were entitled to receive the full amount of the maximum permitted levy amount, equal to the net assessed value available to the taxing unit times the tax rate. (Similarly, rate limited funds were entitled to receive the full amount of money that the available net assessed value, multiplied by the tax rate, would produce.) The tax caps added an additional limitation on the amount of money that a fund could receive, by placing a limit on the maximum percentage of gross assessed value that could be imposed on the various classes of taxable property.

When tax caps are exceeded, various funds experience a reduction in the amount of money they receive. That reduction can be eliminated if enough additional assessed value is made available to the taxing unit to bring the tax rates low enough to eliminate the loss due to the impact of the tax caps (since, all other things being equal, the more assessed value available, the lower the tax rate can be).

As a general matter, anything that either increases available net assessed value or reduces the tax rate below the tax caps will have the effect of restoring all or part of the loss created by the tax caps.

Many factors can affect the level of the assessed value available to a taxing unit. Such factors include, among others, the success of the taxing unit in attracting new investment that adds to the tax base; loss of businesses; the continued existence of an existing TIF District (that, if terminated, would free up assessed value for the underlying taxing units); State law policies relating to exemptions of various classes of property from taxation; the right of a taxpayer in certain cases to receive a deduction in the assessed value of taxable property; local tax assessment practices; and transfers of taxable property to non-taxable owners.

Many factors can impact whether tax caps will be exceeded, including, among others, the existence or increase in the amount of debt payable from property taxes that is incurred by any of the overlapping taxing units; the existence or creation of a cumulative capital fund; the tax rates of other overlapping taxing units; and access to other, non-property tax sources of funds, such as local income taxes or various revenues from the State.

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