

Summary of School Finance Options

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QUICK REFERENCE FOR PUBLIC FINANCE ISSUES

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This provides an overview of the financing options available to school districts and summarizes the process districts must follow to borrow money.

INTRODUCTION

Mississippi school districts periodically must borrow money to finance construction, repairs, acquisitions and operations. School districts may borrow money only in the manner and for the purposes allowed by law. The authorizing statute may describe the district's written obligation to repay the debt as a bond, note, lease or other written obligation. Regardless of how the written obligation is described, the obligation is simply the written promise of the district to repay a loan. This document summarizes the primary types of debt school district may incur and summarizes related matters districts should consider when issuing debt. Interest paid by a district on its debt may be exempt from state and federal income taxes, if the district complies with the applicable tax regulations. Issuing the debt as tax-exempt debt allows the district to finance projects at a reduced interest cost. A discussion of the applicable tax regulations is beyond the scope of this module.

Mississippi law allows districts to issue each of the following types of debt. Each type has certain advantages and disadvantages. The best alternative for a district in any situation will depend on several factors, including the district's debt limit, financial situation, the project to be financed and anticipated future needs. Due to debt limitations, a district may need to issue more than one type of debt to finance a project.

GENERAL OBLIGATION BONDS

MS Code 37-59-1 through 37-59-45

Purpose –

School districts typically issue general obligation bonds to finance large capital improvement projects. Bond proceeds may be used only for statutorily permitted purposes, including, among other things:

- (1) Purchasing, constructing, renovating and equipping school facilities and athletic fields, and purchasing land for such purposes; and
- (2) Providing necessary water, light, heating, air conditioning and sewerage facilities for school facilities

Debt Limit –

A district may have more than one general obligation bond issue outstanding at any time, but the total amount of outstanding general obligation bonds generally may not exceed 15% of the assessed value of taxable property within the district. A district may issue bonds exceeding the 15% debt limit if the district's enrollment has increased by at least 20% over the last five years, or if at least nine percent of the area of the district's land is in a flood control reservoir or in a national forest, or if the district's assessed value per pupil is less than 75% of the state-wide average assessed value per pupil.

Only a district's outstanding general obligation bonds count against the 15% debt limit. A district's outstanding notes and leases do not count against the limit. Furthermore, bonds secured by a pledge of a district's education enhancement fund money for buildings and buses do not count against the debt limit. A district can therefore effectively exceed the 15% debt limitation to the extent it pledges its education enhancement funds for buildings and buses to repay a portion of the bonds.

A district must obtain voter approval in a bond referendum before issuing general obligation bonds. Therefore, a practical limit on the amount of bonds to be issued is the political question of how large a millage increase the voters will accept to repay the bonds. For many districts, this political consideration may be a greater limit on the amount of bonds than the 15% statutory limitation.

Conduct of Election –

After settling on the project to be financed and the amount of bonds to be issued, the school board initiates a bond issue by adopting two resolutions: a resolution of intent and an election resolution. The resolution of intent states the maximum amount of bonds the board intends to issue and describes the project the board intends to finance if the bond proposition is approved in a bond referendum. The resolution of intent also contains certain other statutorily required findings. The board then adopts a resolution calling a special election on whether the bonds should be issued. The election resolution states the date of the election, describes the bond proposition, names the polling places to be used and approves the form of the ballot to be used in the election. The board may call for the election to be held either at the regular city or county polling places or at one or more schools.

The bond election may be held at the same time as a general election or may be held on another date. In either event, the election constitutes a special election, since the board has the discretion over when to call the election and where it is to be held. The ballot must describe the amount and purposes of the proposed bond issue and must include the words "FOR THE BOND ISSUE" and "AGAINST THE BOND ISSUE" and a place for the voter to mark his or her vote.

After the school board adopts the resolution of intent and the election resolution, the board turns the process over to the appropriate election commission to conduct the election. According to an opinion of the Mississippi Attorney General, the city election commission is to conduct a bond election on behalf of a municipal school district and the county election commission is to conduct a bond election on behalf of a county school district. The appropriate election commission is statutorily required to conduct the bond election to the extent practicable in the same manner as other city or county elections.

The district is responsible for publishing a notice of the bond election for at least three consecutive weeks before the election in a newspaper published in the district. If no newspaper is published in the school district, the notice must be published in a newspaper having a general circulation if the school district.

After the polls close on election day, the election commissioners canvass the ballots and certify the election results to the school district. Based on the certified election results, the school board adjudicates whether the bond proposition received the necessary 60% approval.

After a bond election passes, but before the bonds are sold, the school board may call an election requesting authority to either amend the proposed use of bond proceeds or to revoke its authority to issue the bonds. The election must be held in the same manner as detailed above.

Security for Bonds; Education Enhancement Fund Pledge –

General obligation bonds are secured by the full faith and credit of the district and are payable from the avails of an unlimited, special tax to be levied on the property of the district for the sole purpose of repaying the bonds. The district should include the amount of the necessary bond payments in the annual tax levy request to its levying authority. The school district's levying authority must levy a sufficient tax to repay the principal of and the interest on the bonds.

A school district may also pledge its Education Enhancement Funds received from the State for building and buses for the repayment of general obligation bonds.

Limitations on the terms and details of the bonds –

Except as stated in the following sentence, general obligation bonds must mature annually over a term not exceeding 20 years. If the bonds are issued in any year after taxes are levied, the first principal payment must be made within two years from the date the bonds are issued. At least two percent of the original bond principal must mature in each of the first five years of the issue, and at least four percent of the principal amount must mature in each of the following ten years.

The bonds may not bear interest at a rate greater than the maximum statutorily allowed interest rate (11%). No bond may bear more than one rate of interest, and each bond must bear the state rate of interest until maturity. All bonds of the same maturity must bear the same rate of interest, and accrued interest must be paid annually or semiannually. The lowest interest rate for any bond must not be less than seventy percent of the highest interest rate on the bonds, and each interest rate must be in multiples of either one-eighth of one percent or one-tenth of one percent. MS Code Sections 37-59-25 and 37-59-27 contain other limitations on the details and terms of general obligation bonds.

Limitations on the use of proceeds –

A district may use bond proceeds only for the purposes stated on the bond ballot. School officials may be held liable for any misuse of bond proceeds. The bond ballot should, therefore, be drafted carefully and the district should ensure the proceeds are spent on permitted purposes. A school district must use any bond proceeds remaining in the special fund after the approved project is completed to repay any outstanding bonds.

LIMITED-TAX

MS Code 37-59-010 through 37-59-115

Limited-tax notes are typically easier for a school district to issue than general obligation bonds, since an election is not required as a prerequisite to issuing the notes. An election is required only if petitions are filed by the requisite number of voters calling for an election on the issuance of the notes. Such petitions are rarely filed. The limited tax to repay the notes, however, limits the amount a district may borrow through notes.

Purposes; Resolution of Intent; Election –

Districts may issue limited-tax notes to finance:

- (a) Constructing, repairing, improving or equipping school buildings and athletic facilities, and purchasing land therefor, and
- (b) Purchasing heating plants, air conditioning, fixtures, equipment for school buses and transportation equipment

Note proceeds may also be used to refinance outstanding notes, if a lower interest rate will be secured on the outstanding notes. A school board initiates a note issue by adopting a resolution declaring the following statutorily prescribed matters: (1) the necessity for and its intention of borrowing money, (2) the amount to be borrowed, (3) the nature and approximate cost of the project and, (4) that no funds are otherwise available to pay for the project. The resolution must be published in a newspaper of general circulation in the district, with the first publication being at least fifteen days before the date when the school board plans to authorize the issuance of the notes. Unless petitions containing the names of 20% of the district's voters are filed calling for an election, the board may proceed to issue the notes.

Levy of Special Tax; Pledge of Education Enhancement Funds –

A school district's levying authority must annually levy an ad valorem tax, not to exceed three mills, to pay debt service on all outstanding limited-tax notes of the district. A school district should include the necessary debt service amount when requesting its levying authority to levy taxes on behalf of the district. As a practical matter, since most ad valorem taxes are collected between January and March of each year, if feasible, a district should schedule the first payment on its notes to occur between March and the end of the tax year.

Restrictions on Issuance –

Limitations on indebtedness

The annual tax levy for all outstanding limited-tax notes of a school district may not exceed three mills on all taxable property in the school district. Limited-tax notes are not subject to any other statutory school debt limitation.

A TAN must be repaid within fourteen months and may not bear interest at a rate greater than 11%.

Agricultural high schools may also issue TANs, with the most notable distinction being that agricultural high schools may not borrow more than fifty percent of the anticipated amount of taxes to be collected against which such funds are borrowed.

SHORTFALL NOTES

MS Code 37-57-108

A district may issue a shortfall note to make up any difference between the amount of revenues the district requested from its levying authority and the actual amount it receives in a fiscal year. The principal amount may not exceed the estimated amount of the shortfall and may not exceed twenty-five percent of the school district's fiscal year budget for the fund in which the shortfall occurs. The district should use the form promulgated by the Office of the State Auditor in calculating the amount of the shortfall. The school district is not required to publish notice of its intent to issue the notes, and no election is required. The notes must otherwise be issued in accordance with the procedure provided for in MS Code section 27-39-333.

The note proceeds must be applied to the fund in which the shortfall occurred. The interest rate on the notes may not exceed 11%. The notes must be repaid in equal installments within three fiscal years. The levying authority must levy a special ad valorem tax to repay the notes.

QUALIFIED ZONE ACADEMY BONDS

Qualified Zone Academy Bonds ("QZABs") are interest free loans governed predominantly by federal tax law, a discussion of which is beyond the scope of this presentation. A district with QZAB authority must issue the QZAB as a note, bond or lease under the state law authority already discussed. If the district satisfies the federal QZAB regulations, the note, bond or lease will constitute a QZAB for federal tax purposes. The district does not pay interest on a QZAB loan. Instead, the lender receives a tax credit on its federal income tax. The following is an abbreviated summary of QZABs.

Congress periodically authorizes the issuance of a limited amount of QZABs by public school district within each state. Mississippi typically receives an annual QZAB allocation of \$4,000,000 to \$6,000,000. The Mississippi State Department of Education allocates the QZAB borrowing authority among school districts within the state on a first come, first served basis.

A district receiving an allocation to issue a QZAB must follow state law requirements for issuing the debt and must also comply with the federal tax regulations. In particular, under federal tax law, the QZAB proceeds generally may be used only for renovating, repairing or equipping an existing school designated by the school board as an academy. The academy must either be located in an empowerment zone or at least 35% of its students must qualify for free or reduced lunch. The district must obtain written assurance that it will receive a contribution for the academy from one or more private sources. The contribution must have a present value equal to at least 10% of the amount of the QZAB borrowing. Furthermore, the school district must prepare a comprehensive education plan for the academy.

The Stimulus Bill passed in 2009 allows school districts to issue notes, bonds and leases as Qualified School Construction Bonds (“QSCBs”) if the debt meets the federal tax law requirements. The QSCBs have favored treatment under the tax law, in that the district pays little or no interest on the QSCBs. Instead, either the lender takes a federal tax credit in lieu of interest or the federal government subsidizes interest payments made by the district. QSCBs are more flexible than QZABs, in that QSCB proceeds may be used for broader purposes and the contribution and the education plan required for QZABs are not required for QSCBs.

TRANSPORTATION NOTES

MS Code 37-41-89 through 37-41-99

School districts may also issue transportation notes to pay the costs of certain transportation equipment and buses, with the approval of the State Board of Education. The notes must mature within six years and are repaid from the district’s transportation funds. No election or other approval is required for the issuance of the notes.

REFUNDING BONDS AND NOTES

MS Code 31-27-1 through 31-27-25

School districts may issue bonds to refinance outstanding debt, as long as the refinancing will produce a net, present value savings equal to at least 2% of the debt being refinanced. The district is not required to hold an election or to obtain any other approval to refinance the debt. The refinancing bonds generally have the same term and security as the debt that is being refinanced.

ENERGY EFFICIENCY LEASE

MS Code 31-7-14

A district may finance energy efficiency improvements to existing buildings through a lease purchase arrangement. The term of the lease may not exceed 15 years. The lease is to be repaid from energy savings obtained by making the improvements. The district must issue a request for qualifications to select the contractor to make the improvements. The district may require the contractor to guarantee the savings necessary to make the lease payments.

EQUIPMENT LEASE

MS Code 31-7-13(e)

A district may lease purchase equipment under MS Code Section 31-7-13(e) or through a related State master lease program. The term of the lease may not exceed the useful life of the equipment. No election or other approval is required before entering into the lease financing. The lease must contain an annual appropriation clause and must be repaid from any available funds of the district.

OTHER RESTRICTIONS AND LIMITATION GENERALLY APPLICABLE TO SCHOOL DEBT

A district may need to consider and address some of the following matters relating to the issuance of school debt.

Open Meetings Requirements –

All actions of a school board authorizing debt must be taken at meetings that comply with Mississippi open meetings laws.

Public Bid Requirements –

A district must generally advertise debt for sale upon the receipt of sealed bids, unless otherwise authorized to sell its bonds through a private sale. The notice of bond sale must be advertised at least two times in a newspaper published in the county in which the district is located. The first publication of the notice must be made not less than ten days before the deadline to receive bids. Each bid must include a cashier's check, issued or certified by a bank located in Mississippi, equal to at least two percent (2.0%) of the par value of the bonds offered for sale.

Validation Proceedings –

A district may submit its debt for validation by the appropriate chancery court as provided in Mississippi's bond validation statute. In practice, the determination of whether to submit the debt for validation generally turns on the size and complexity of the issue. Upon a final decree validating the bonds (including any appeals thereof), the validity of the debt will "be forever conclusive against" the public entity issuing the bonds, and the validity of the bonds "shall never be called in questions in any court in this state."

OTHER STATE AND FEDERAL LAWS

Voting Rights Act –

Section 5 of the Voting Rights Act of 1965 requires Mississippi public entities to submit any "change affecting voting" to the United States Department of Justice for pre-clearance before implementing the change. Applicable regulations identify a special election (such as a bond election) as a "change affecting voting." Therefore, school district must submit a special bond election to the Department of Justice for approval in order for the election results to be effective.

Securities Laws –

School districts must comply with Mississippi and federal securities laws when issuing debt.

Federal Tax Laws –

The Internal Revenue code and related regulations restrict the issuance of tax-exempt bonds.

Mississippi Constitution –

Certain provisions of the Mississippi Constitution may indirectly limit the issuance of bonds by a public entity. For example, Article 7, § 183 and Article 14, § 258 prohibit a public entity from donating its credit to a private entity, and Article 4, § 109 prohibits a public official from having a pecuniary interest in contracts (such as bonds) authorized by the public body on which board he serves.

Desegregation laws –

Many school districts are subject to a federal court desegregation order. The desegregation order may require court approval before the financing, construction or purchase of school facilities.