

Legislative Analysis



QUALIFIED REFUNDING OBLIGATIONS

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House Bill 4248 without amendment

Sponsor: Rep. Matt Huuki

Committee: Commerce

First Analysis (2-22-11)

BRIEF SUMMARY: The bill would allow an eligible municipality to restructure debt payments owed by a downtown development authority. Generally speaking, the bill allows, among other things, a municipality to restructure DDA debt by extending debt payments further into the future and lowering current payments. According to committee testimony, the bill applies to the DDA in the City of Houghton in the Upper Peninsula.

FISCAL IMPACT: House Bill 4248 would have an indeterminate fiscal impact on local units of government. The bill expands the instances in which qualified refunding obligations may be used. Refunding obligations are issued to restructure or refinance the costs of an earlier debt obligation. The new obligations are often associated with lower interest and/or payment costs to the municipality or authority. Under this bill, a municipality could see reduced payments in the short run but higher costs in the long term as a result of issuing refunding obligations that extended debt further into the future.

THE APPARENT PROBLEM:

The Downtown Development Act is aimed at stimulating economic development in business districts. It is a tax increment finance statute. When local units of government create a tax increment financing authority, or TIFA, they typically establish a special district and then capture future increases in taxes within that district for the authority to use to finance public infrastructure improvement projects within the district; this can include the issuance of bonds to finance projects. The DDA is one of several statutes that allow for the creation of TIFAs.

When TIFAs are created, the expectation is that property values within the special district will grow so as to provide revenue sufficient to make payment on any debt issued. The recent unanticipated reduction in property values has produced reduced property tax collections. In some cases, communities are finding that the incremental revenues that were anticipated to cover debt payments are not materializing. This problem has been compounded in the City of Houghton's DDA, according to committee testimony, because its scheduled debt payments are due to increase substantially this May and because a building previously on the tax rolls has been purchased by Michigan Technological University, further reducing revenue. There are restrictions in statute on when certain bond issues can be refunded or refinanced. This includes requiring a net present value interest saving when debt is refinanced. However, in the circumstances faced by Houghton, restructuring of debt is needed to reduce current debt payments and extend debt further into the future. The bill would allow this under certain specified conditions.

THE CONTENT OF THE BILL:

House Bill 4248 would amend the Downtown Development Authority Act (MCL 125.1651) to do the following:

****** It would revise the definition of "qualified refunding obligation" in order to add an additional case when DDA debt obligations can be refinanced. The specific descriptions in the bill apply to the City of Houghton in the Upper Peninsula.

Specifically the bill would allow a refunding obligation to be issued if:

The obligation is issued to refund an "other protected obligation" [originally] issued as a capital appreciation bond delivered to the Michigan Municipal Bond authority on December 21, 1994, and any subsequent refunding of that obligation issued before January 1, 2012.

(However, the bill would only apply to the extent that tax increment revenues to repay the qualified refunding obligation that stem from state and local school taxes and from state appropriations to make up for lost school revenue do not exceed \$750,000.)

The term "other protected obligation" is a technical term in the act. Since the passage of Proposal A to fund public schools in 1994, downtown development authorities have been generally prohibited from capturing taxes that are used to fund school districts, except in cases specified in the law where obligations (e.g., bonding arrangements) were entered into before or during the implementation of Proposal A. These are known as "eligible obligations" and "other protected obligations." The definitions of these terms have been subsequently expanded to also apply to the refunding of those kind of obligations in certain circumstances.

****** In addition, the bill also specifies that qualified refunding obligations issued under the bill before January 1, 2012, would not be subject to certain requirements of the Revised Municipal Finance Act (found at Sections 305 (2), (3), (5), and (6); Section 501; Section 503; and Section 611).

This means the refunding obligations issued under the bill would not be subject to the requirement that municipal securities not be sold at a discount exceeding ten percent of the principal amount of the security, or to requirements related to maturity dates and redemption dates. They also would be exempt from the prohibition on issuing refunding obligations unless the net present value of the principal and interest to be paid on the refunding security is less than the net present value of the principal and interest to be paid on the security being refunded.

****** The duration of the development program described in the tax increment financing plan that relates to the qualified refunding obligations issued under the bill would be extended to one year after the final date of maturity of the obligations. The obligation would be payable through the year 2025 at an interest rate not exceeding the maximum

rate permitted by law, notwithstanding the bond maturity dates contained in the notice of intent to issue bonds published by the municipality.

BACKGROUND INFORMATION:

It should be noted that Public Act 321 of 2010 (House Bill 5550) amended the Revised Municipal Finance Act to allow municipalities to refund debt before December 31, 2012, without regard to the "net present value" requirement, but only with the approval of the Department of Treasury and only if the securities are not secured by the unlimited full faith and credit pledge of the municipality. Several companion bills (House Bills 5551-5554) were not enacted, however. One of those, House Bill 5552, would have amended the Downtown Development Authority Act in a manner similar to the bill under discussion. Also House Bill 6251 of last session specifically dealt with the case at issue in this bill. HB 6251 passed the House and was reported to the floor of the Senate, but was not acted on before the legislative session ended.

ARGUMENTS:

For:

The bill addresses a special case where tax increment finance revenues in a downtown development authority are not sufficient to make required bond payments. The bill provides exceptions to current law to allow the DDA (in the City of Houghton) to restructure that debt. The bill contains a cap on the amount of school taxes and related state appropriations that can be captured. Similar exceptions have been made in the past, supporters argue. They also note that a very similar bill passed the House and was on the Senate floor when the 2009-2010 legislative session ended.

Response:

Perhaps a comprehensive approach to such problems would be preferable to legislating case by case.

POSITIONS:

The City of Houghton indicated support for the bill.

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