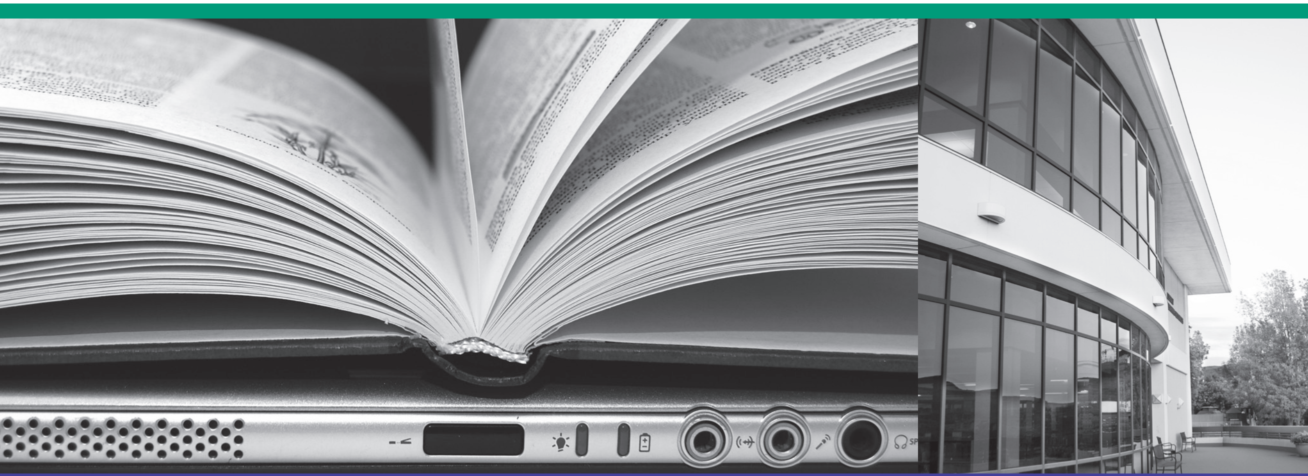
Bond Basics for Library Districts and Other Municipal Libraries in New York State



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Dedicated to the memory
of
A.T. “Tom” Galloway II

Bond Counsel to Libraries
Across New York State

1942–2004

Coach, Mentor, Scholar, Friend
and One Funny Guy
We Miss You

Bond Basics for Library Districts and Other Municipal Libraries in New York State

CHAPTER ONE

Introduction

Public Libraries and Public Library Districts in New York State are generally without authority in current law to directly issue indebtedness in their own name either for capital purposes or in anticipation of the receipt of tax revenues (TANs) or other revenues (RANs) for cashflow purposes (except for mortgage note financings as described in Chapter 9 or pursuant to special legislation.) That is a function of the school district or municipality with which the Library or Library District is affiliated which will hereinafter be referred to as the "Affiliated Entity."

The borrowing of money for various governmental purposes of a school district or municipality in New York State (the "State") including borrowing as an Affiliated Entity on behalf of a Library or Library District, is governed predominantly by the State Constitution and the Local Finance Law, Chapter 33-a of the Consolidated Laws of the State (hereinafter sometimes referred to as the "LFL"). The power to spend the borrowed money to accomplish a valid purpose of the Library or Library District, however, generally derives from other laws, in particular, the Education Law, as well as the General Municipal Law. The focus of this primer is on the restrictions, rules and procedures governing the issuance of debt by school districts and municipalities on behalf of Libraries or Library Districts in the State (other methods of finance by other type libraries are also discussed to a lesser extent). The role of Bond Counsel relates to determination of the validity of debt: valid authorization, valid sale, valid tax and disclosure status, and valid issuance.

The role of Bond Counsel in the issuance of debt on behalf of a Library District or municipal library in a nutshell is thus, as follows:

- Determine that the project is a valid Library District or municipal purpose under New York State law.
- Determine that the project is a capital project eligible for financing.
- Determine the useful life of the project as provided by the State Legislature (regardless of what Bond Counsel and/or the Library may know to be different in actual use).
- Determine that any conditions necessary to be completed prior to adoption of a bond resolution have been properly completed (i.e., compliance with the State Environmental Quality Review Act; drafting of Library District or municipal referendum proceedings).

- Draft the text of the bond resolution in accordance with Local Finance Law requirements and confirm valid adoption. The bond resolution is the legal proceedings of an Affiliated Entity authorizing the issuance of debt for your project.
- Draft the text of the Legal Notice of estoppel of the bond resolution to be published after valid adoption and confirm proper publication.
- Draft the documentation necessary to ensure that the sale of Affiliated Entity bond anticipation notes or bonds is in conformity with requirements of Local Finance Law and the regulations of the office of the State Comptroller.
- Participate in the production of a disclosure document about the Affiliated Entity and its finances and in some cases, the Library District and its finances (the official statement) and work with Library District and Affiliated Entity and financial advisor to be sure it is not less than 100% accurate.
- Determine that the sale and award of debt is in conformity with Local Finance Law and the regulations of the office of the State Comptroller thereunder, and is within the debt limit applicable.
- Draft the actual debt instruments of the Affiliated Entity and the requisite closing documentation, including federal tax law and disclosure law covenants and compliance certifications.
- Provide an opinion of Bond Counsel that, in effect, each of the steps described above was completed in conformity with the laws of the State.

To this end, bond counsel are involved early on in planning either a capital project or a cashflow borrowing for operational expenses. From the beginning, the activities of a Library *prior to borrowing* may have implications under federal tax laws, federal securities laws, the local finance law and/or the state education law.

Without a "bond counsel opinion" from a reputable, knowledgeable firm, preferably one that will exist at least as long as the debt on behalf of a Library is outstanding, a school district or municipality is generally not able to sell its debt because it is that opinion that provides comfort to the purchasers of such debt that it is a valid and binding obligation of the school district or municipality to repay the purchaser both the principal loaned and interest thereon. And although it is debt issued for the benefit of a Library District or a Library, it is the issuer, i.e., the Affiliated Entity, that is ultimately, constitutionally, on the hook to see it paid.

This booklet should serve as a primer for library officials and other interested parties on the basic bond rules governing public libraries and their Affiliated Entities, particularly public library districts affiliated with school districts, and the proper functions of bond counsel. *Some* of these rules should also be applicable to certain free association libraries to the extent they are chartered by the Board of Regents and their budgets are governed by Article 5 of the Education Law but Affiliated Entities cannot issue debt on behalf of a free association library. *See* Chapter 20 for bond financings for free association libraries. Any library subject to the provisions of any special act of the State Legislature needs to review that special legislation with bond counsel initially to determine its establishment status and governing statutes.

If your library is effectively a department of a municipality such as a County, City, Town or Village, you probably submit your budget annually as part of the municipal budget process or have a previously voter approved annual budget, and the municipality levies taxes annually to cover the expenses of your department and the others of the municipality. As such you do not have a separate independent "corporate" existence for financial purposes, despite the fact that you are managed by a Board of Trustees with all power of an educational corporation chartered by the Board of Regents, rather than a department head. In addition, you cannot borrow moneys or levy a tax in your own name. You may, nevertheless, wish to read this primer to understand the constraints under which your municipality operate when borrowing money. And note: you may have a friend of the Library type charitable organization that raises funds for you and indeed as a not-for-profit, they might indeed have the authority to borrow money, although it would be rare for such an organization to have the wherewithal to pledge to encourage a bank to loan to them. If they do, for example, by virtue of a stream annual payments pledged or bequeathed to them, then please read Chapter 20 for more information on not-for-profit library borrowings.

CHAPTER TWO

Constitutional Requirements

Limitations on school district and municipal indebtedness are set forth in Article VIII of the New York State Constitution and are implemented by the Local Finance Law. The provisions of Article VIII are generally applicable to all school districts and municipalities in the State and the obligations authorized by their legislative bodies in their capacity as the finance board. Most local governments including school districts have a constitutionally established debt limit (and those which do not have a statutory limit). In addition, there are constitutionally based rules on the loan of school district or municipal credit, uses of borrowed moneys and the pledge of faith and credit. As a library relying upon another political subdivision to issue "your debt," you need to know the applicable constraints.

Loan of Credit Prohibition

Article VIII, Section 1 of the Constitution provides that no county, city, town, village or school district shall give or loan any money or property to or in aid of any individual or private corporation, association or private undertaking nor shall any such local governmental unit give or loan its credit to or in aid of any of the foregoing or any public corporation. There are limited exceptions to the general rule that local governmental units cannot give or loan money, property or credit for other than governmental purposes, generally relating to health and welfare facilities. The State Legislature has determined that debt issued by an Affiliated Entity for a public library district is not a loan of credit. (The same cannot be said generally for free association library projects which are a variety of public or private (really hybrid) corporation for this purpose.) Incidental private benefit is permissible and there is an abundance of case law on its limitations.

Valid Purpose Requirement

Article VIII, Section 2 of the Constitution provides that no county, city, town, village or school district shall contract indebtedness except for a county, city, town, village or school district purpose, respectively. Each can only borrow money to do things that it is permitted to do. The State Legislature has determined that a library project is a valid public purpose for these units of local government. (The same cannot be said generally for free association library projects which are *not* a valid local governmental purpose). No such indebtedness is to be contracted for longer than the period of probable usefulness of the particular purpose which is legislatively determined by the State in every case (or, in the alternative, the weighted average period of probable usefulness of several purposes if financed in the same obligation) for which it is contracted and in no event may this period exceed forty years.

Pledge of Faith and Credit

Article VIII, Section 2 of the Constitution also provides that each such local governmental unit must pledge its faith and credit and make annual provision for the payment of the principal of and the interest on any of its indebtedness. This is the heart of a "general obligation" bond or note—the ability and promise to tax as necessary to repay the debt. All of the taxable real property within (1) a Library District in the case of Library Districts or (2) the Affiliated Entity in the case of municipal libraries, is subject to the levy of ad valorem taxes (a) by the Affiliated Entity on behalf of the Library District or (b) by the Affiliated Entity as part of its general tax levy in the case of municipal libraries) to pay principal and interest without limitation as to rate or amount. School districts and municipalities in the State are only authorized to issue general obligation type debt. They cannot issue revenue bonds solely backed by a specific stream of revenue or bonds secured by a mortgage on real property or any other type debt instrument including a simple bank loan. (The sole exceptions to the rule are certain lease-purchase obligations subject to appropriation, including energy performance contracts, which cannot involve the pledge of the faith and credit and therefore are not technically debt yet are subject to the same authorization requirements as debt. *See* Chapter 17 herein. Note also that while school districts and municipalities cannot mortgage property, a Library District can. *See* Chapter 9 herein.)

Except for certain short-term indebtedness contracted in anticipation of the collection of taxes and indebtedness to be paid within one of the two fiscal years immediately succeeding the fiscal year in which such indebtedness was contracted, all indebtedness must be paid in annual installments of principal. Indebtedness must be paid in annual installments commencing not more than two years after the debt was contracted and no installment may be more than fifty percent (50%) in excess of the smallest prior installment unless the legislative board provides for and utilizes substantially level or declining annual debt service payments. It is never possible to skip a year in the paydown of borrowed amounts after the first anniversary of the first borrowings.

Annual Appropriation

Provision must be made annually by appropriation by the Affiliated Entity for the payment of interest on all of its indebtedness and for the amounts required for the amortization and redemption of its serial bonds (and hence the Library District must covenant and contract to make such payments to that Affiliated Entity). If at any time the respective appropriating authorities fail to make such appropriations, a sufficient sum must be set apart from the first revenues thereafter received (by your Affiliated Entity which issued the debt) to be applied for debt service and may be so required at the suit of any holder of a debt obligation; however, this latter Constitutional provision does not apply to revenue anticipation notes, tax anticipation notes, or bond anticipation notes, discussed later in this primer.

Debt Limits

Article VIII, Section 4 of the Constitution provides that no county, city, town, village or school district shall contract indebtedness which, including existing indebtedness, shall exceed seven percent (7%) of the five year average full valuation of taxable real estate therein. (There are some exceptions to this, most notably, cities having 125,000 inhabitants or more (except New York City), nine percent (9%), and any small city school district, five percent (5%). Central and union free school districts are statutorily limited to ten percent (10%).) The average full valuation of taxable real estate of the respective governmental unit is determined pursuant to Article VIII, Section 10 of the State Constitution by taking the assessed valuations of taxable real estate on the last completed assessment roll and the four preceding rolls and applying to such rolls the ratio (as determined by the State Office of Real Property Services) which such assessed valuation bears to the full valuation. Article VIII, Section 5 and Article VIII, Section 2-a of the State Constitution enumerate exclusions and deductions from the Constitutional debt limit. Such exclusions include, for example, self-liquidating debt, indebtedness incurred for water and certain sewer facilities, as well as typical cashflow borrowings hereinafter described. Debt issued on behalf of a Library District is technically included in the calculation of the net indebtedness of an Affiliated Entity.

There are also numerous exclusions and deductions in the debt limit calculations particular to each type of governmental unit. Inasmuch as very, very few, if any, school districts, other than small city school districts or municipalities, ever approach their debt limit, these exclusions and deductions will not be discussed in detail here. (City school districts have more deductions and fewer exclusions than central and union free school districts. While central and union free school districts may exclude from their debt limit an amount equal to the current year building aid estimate, small city school districts may not. However, unlike central and union free school districts, small city school districts need not include in their debt limit calculations any debt which has been refunded (refinanced through a new issuance of bonds).)

Tax Limits

It is significant that there is no constitutional limitation on the amount that may be raised by a school district or municipality by tax upon real property in any fiscal year to pay principal of and interest on its indebtedness. Indeed, the State is specifically precluded from restricting the power of any local government to levy taxes on real property for this purpose in Article VIII, Section 12 of the Constitution. This is the firm basis upon which general obligation debt rests that, together with sound fiscal practices and the resultant bond rating, permits an Affiliated Entity to borrow at advantageous tax-exempt interest rates to the benefit of the Library District.

CHAPTER THREE

General Implementing Statutory Provisions

Sections 100.00 and 101.00 of the Local Finance Law contain the statutory counterparts of the Article VIII Sections 1 and 2 Constitutional provisions described above. They read simply and clearly:

"§100.00 Requirement of pledge of faith and credit

Every municipality, school district and district corporation shall pledge its faith and credit for the payment of all indebtedness contracted by it."

"§101.00 Giving or loaning of municipal credit and contracting indebtedness other than for municipal purposes prohibited

a. No municipality, school district or district corporation shall:

1. Give or loan its credit to or in aid of any individual, or public or private corporation or association, or private undertaking, or

2. Contract indebtedness except for the purposes of such municipality, school district or district corporation.

Notwithstanding the foregoing provisions of this paragraph:

1. If any municipality or any county or town on behalf of an improvement district is authorized by a general law or by a special law (a) to provide a supply of water, in excess of its own needs, for sale to any other public corporation or improvement district, (b) to provide facilities, in excess of its own needs, for the conveyance, treatment and disposal of sewage, from any other public corporation or improvement district, or (c) to provide facilities, in excess of its own needs, for drainage purposes from any other public corporation or improvement district, the indebtedness contracted by the municipality for such an object or purpose shall be deemed to be for a county, city, town or village purpose, as the case may be.

2. If any two or more municipalities and county and town improvement districts are authorized by a general law or by a special law (a) to provide for a common supply of water, (b) to provide for the common conveyance, treatment and disposal of sewage or (c) to provide for a common drainage system, the joint indebtedness, or the several indebtedness for a specific proportion of the cost, contracted by the municipality for such an object or purpose shall be deemed to be for a county, city, town or village purpose, as the case may be.

> 3. If any two or more municipalities and school districts and county and town improvement districts are authorized by a general law or by a special law to join together to provide any municipal facility, service, activity or undertaking which each of such units has the power to provide separately, the joint indebtedness, or the several indebtedness for a specific proportion of the cost, contracted by the municipality or school district for such an object or purpose shall be deemed to be for county, city, town, village or school district purpose, as the case may be."

There are exceptions to this rule particular to each of the various municipal units of government. Additionally, Title 8 of the Local Finance Law contains the statutory limitations on the power to contract indebtedness and includes central and union free school districts not covered by the constitutional provisions. Section 104.00 limits, in accordance with Article VIII, Section 4 of the Constitution, the ability of local governmental units to contract indebtedness to the respective Constitutional percent of the five year average full valuation of taxable real estate. The statutory provisions implementing Constitutional provisions authorizing deductions and excluding indebtedness from the debt limits are found in Title 9 and Title 10 of the Local Finance Law. In addition to the Constitutionally enumerated exclusions and deductions, deductions are also allowed for cash or appropriations for debt service pursuant to the authority of a decision of the New York Court of Appeals, the State's highest court.

Protection of Holders of Local Government Debt in the State

Holders of the debt instruments of local governmental units in the State are the beneficiaries of both Constitutional and statutory protections. The pledge of the faith and credit of the issuer is taken very seriously in the State. There is no known occurrence of an absolute default in the payment of general obligation debt in the State in the past 100 years or more. Rating agencies, insurance companies, bond mutual funds, and banks all know this which helps to keep the interest rates the Affiliated Entities pay on their debt (including, "your" debt) in New York relatively low in comparison to non-general obligation debt.

Contract Remedies

In addition to Constitutional provisions discussed in Chapter 2, debt holders have additional statutory protections. The General Municipal Law of the State provides that it shall be the duty of the governing board, to assess, levy and cause to be collected a sum of money sufficient to pay a final judgment for a sum of money or judgment directing the payment of money which has been recovered against the governmental unit and remains unpaid. The General Municipal Law further provides that the rate of interest to be paid by a municipal corporation upon any judgment against a municipal corporation shall not exceed the rate of nine per centum per annum. This provision might be construed to have application to the holders of local governmental debt in the event of a default in the payment of principal of and interest. Execution or attachment of property cannot be obtained to satisfy a judgment by holders of general obligation indebtedness of any school district or municipality.

The Federal Bankruptcy Code allows public bodies recourse to the protection of a Federal Court for the purpose of adjusting outstanding indebtedness. Section 85.80 of the Local Finance Law contains specific authorization for any "municipality" in the State to file a petition under any provision of Federal bankruptcy law for the composition or adjustment of municipal indebtedness. School districts are not included in the Local Finance Law definition of "municipality."

At the Extraordinary Session of the State Legislature held in November, 1975, legislation was enacted which purported to suspend the right to commence or continue an action in any court to collect or enforce certain short-term obligations of The City of New York. The effect of such act was to create a three-year moratorium on actions to enforce the payment of such obligations. On November 19, 1976, the Court of Appeals, the State's highest court, declared such act to be invalid on the ground that it violates the provisions of the State Constitution requiring a pledge by such City of its faith and credit for the payment of such obligations.

As a result of the Court of Appeals decision, the constitutionality of that portion of Title 6-A of Article 2 of the Local Finance Law enacted at the 1975 Extraordinary Session of the State Legislature authorizing any city, county , town or village with respect to which the State has declared a financial emergency to petition the State Supreme Court to stay the enforcement against such municipality of any claim for payment relating to any contract, debt or obligation of the municipality during the emergency period, is subject to doubt.

The State Aid Intercept

In the event of a default in the payment of the principal of and/or interest on school district obligations only, the State Comptroller is required to intercept and withhold, under certain conditions prescribed by Section 99-b of the State Finance Law, state aid and assistance to the school district and to apply the amount thereof so withheld to the payment of such defaulted principal and/or interest. This requirement constitutes a covenant by the State with the holders from time to time of school district obligations.

If a school district is the library's Affiliated Entity, this rule will apply to its bonds issued on behalf of the library with regard to *any* state aid to the school district.

State Finance Law Section 99-b has always been a comfort to investors and to the credit agencies in rating school district debt in the State.

In the legislative history of Section 99-b, then counsel to State Comptroller Arthur Levitt, Alfred W. Haight., Esq., noted:

> "In the event of a default and a filing of a verified statement of such default with the State Comptroller, he is required to investigate and prepare a certificate setting forth his determinations, and to serve a copy of such certificate with respect to such default upon the chief fiscal officer of such defaulting public body, and to file the original of such certificate in the office of the State Comptroller."
>
> "Immediately after the filing of such certificate, the Comptroller is required to deduct and withhold from the next succeeding payment of State aid due such public

body the amount such city, city school district or school district then in default. If such amount is insufficient, he is also required to deduct from succeeding allotments of State aid due such public body the amounts required to pay all of the principal of and interest on such bonds and notes then in default. The Comptroller is required to forward payments of such moneys to the paying agent for the bonds and notes in default, and to notify the chief fiscal officer of the public body of any payments made to the paying agent on the defaulted obligations of such public body."

"It is anticipated that the additional security that will be provided for school district bonds and notes by the provisions of the proposed act will strengthen all school district bonds and notes and make them more readily marketable."

Louis J. Lefkowitz. Esq., then Attorney General advised then Governor Nelson Rockefeller in a memorandum:

"The bill embodies a covenant by the State with the purchaser of school bonds and notes that it will not repeal, revoke or rescind the provisions of this new section so as to impair the remedies granted thereby. There is a proviso that this, however, is not to be deemed a commitment by the State to continue State aid to any school district."

"This bill is in harmony with the constitutional provision requiring first revenues to be applied by school districts for the payment on indebtedness, in the absence of appropriation for such payments (Art. VIII. Section 2; of Article VII, Section 16)."

Regardless what State Comptroller Arthur Levitt said in 1957—"No bondholder has ever lost a penny through default of any bond issued by a New York State school district"—is as true today as it was over fifty years ago and it is equally applicable to school district debt issued on behalf of library districts.

CHAPTER FOUR

The Library District Referendum Process

The Library District referendum process is a perquisite to the actual authorization of debt financing for your library project in Library Districts. The actual authorization will be accomplished by the adoption of a bond resolution by the legislative body of your Affiliated Entity. See Chapter 6 herein for a discussion of the elements of that bond resolution.

In the case of public libraries which are departments of a municipality, a referendum is not a prerequisite to adoption of the bond resolution although a referendum may be required thereafter. Keep Reading.

Procedural Rules Regarding Bond Resolutions. The steps to be taken prior to and subsequent to adoption of a bond resolution depend on the type of local governmental unit authorizing the debt. In all cases, however, the first step is compliance with the State Environmental Quality Review Act ("SEQRA") and the regulations promulgated thereunder. One of the easiest ways for an opponent of a project to challenge it is for failure to properly comply with SEQRA. The bond resolution itself should specify the previously determined status under SEQRA of the capital project whose financing is authorized by it. Each pre or post bond resolution step, such as the notice of vote should likewise state SEQRA status, including the original notice of a Library District election.

An implementing bond resolution after the referendum must be adopted by two-thirds of the voting strength of the governing board. Voting strength means total membership, not just those present. While this is necessary to implement a successful Library District vote, no one knows what would happen if a school district refused.

The third step is publication of an estoppel notice as described in Chapter Eight. Let us begin then with the referendum process, after completion of compliance with SEQRA.

Coordination of Proposition Language and Bond Resolution Language and Problem Language

The language of a proposition determines how a project is described in a bond resolution and how a project is described in a bond resolution determines how the money can be spent.

The language must be very carefully drafted and consistent.

With library building reconstruction projects involving multiple facilities, it is best to authorize the aggregate cost of a class of objects or purposes rather than specific projects at each library facility. Sometimes, however, local circumstances do dictate that a particular improvement be named in order to garner sufficient public approval of the program. If this cannot be handled in the public relations materials alone, then it may be necessary in the proposition and it will limit flexibility in the allocation of the authorized amount later on.

Propositions should not present alternatives or contain contingencies or options, and certain terminology is mandatory or a proposition will be invalid for purposes of issuing indebtedness. Thus, bond counsel is always best is involved at an early stage of drafting election documents.

Proposition Language

A typical capital project proposition for a new library facility in a Library District with a school district Affiliated Entity would be as follows:

> **LIBRARY BUILDING BOND PROPOSITION**
> Shall the following resolution be adopted, to-wit: RESOLVED, that the Board of Trustees of the Otis Redding Memorial Public Library is hereby authorized to construct a new library addition on Library-owned land located on Dock Avenue in Central Bay, New York adjacent to the existing Library Building, together with reconstruction thereof, including original furnishings, equipment, machinery, apparatus, appurtenances and incidental site and other improvements and expenses therewith, to be operated by the Board of Trustees of the Otis Redding Memorial Public Library, at a maximum estimated cost of $1,700,000 and to expend $200,000 current funds of the Library District therefor; to authorize the Central Bay Union Free School District to borrow or issue obligations in the remaining amount of $1,500,000 (together with renewals thereof) or as much thereof as may be necessary, and for Central Bay Union Free School District to raise by the levy of a tax upon the taxable real property within said School District's boundaries, such amount to said School District for the Otis Redding Memorial Public Library as is necessary for said Library to annually pay principal, interest and premium, if any, on such borrowing or obligations, but in no event an annual amount greater than $250,000.

Note what the proposition approves:

(a) a capital project, (b) its maximum estimated cost, (c) its complete sources of funding, and (d) an increase in the tax levy to cover the highest annual debt service anticipated in the financing of the project. *These elements are all essential if bonding is proposed.*

In any case in which financing through the Dormitory Authority of the State of New York is contemplated, certain additional proposition language is required. *See* Chapter 21 herein.

In any case in which capital reserve fund moneys are expected to form part of the plan of finance, authorization to spend a specific amount of the capital reserve fund needs to also be part of the proposition language.

While contingent language *within* a proposition would be ill-advised, it is permissible to have dependant, linked propositions if the linkage is presented simply and clearly. For example, a second bond proposition can include language that its implementation is predicated on successful approval of the first bond proposition, at the same election. If proposition number one is unsuccessful, then proposition number two is null and void even if successful. This is a particularly useful technique if one element of a capital program is controversial, particularly expensive, or not really as necessary as the other elements. It does also provide something for the voters to reject, which can be a positive or a negative from the point of view of the Board of Trustees.

Referenda In School Districts

In school districts, the Library District must request that the school district Affiliated Entity either call a special election or add a library proposition at the school district's annual election to (a) approve the project, (b) approve its cost, (c) approve the bonding and expenditure for any other funds therefor, and (d) increase the tax levy of the Library District sufficiently to cover annual debt service on the school district debt obligations to be issued on behalf of your library, See Chapter 19 for further details on the referendum proceedings and beyond for Library District with school district Affiliated Entities, as well as our *Bond Basics for School Districts in New York State*.

The referendum occurs before the adoption of the bond resolution in most types of school districts.

Referenda In Towns and Villages

In towns and villages, most commonly, the public library is not a public library district, it is a department of municipal government, albeit with its own Board of Trustees instead of a single department head. If this is your story, then your library will need to work with your Town Board or Village Board of Trustees and get them to adopt a bond resolution authorizing your project and its financing. That bond resolution will usually be adopted subject to permissive referendum, meaning a petition can be filed by taxpayers to disapprove the bond resolution and render it ineffective. (If the library project is to be financed over not more than five years then there is no referendum required or permitted.) Alternatively, a town board or village board of trustees can, after adoption of a bond resolution, call for a referendum on it *on their own motion*. This is an option in cases in which the political powers that be are unsure of popular support for your library project and wish to place the responsibility on to the taxpayer themselves to decide. See our *Bond Basics for Towns, Villages and Cities in New York State* for more information on this process.

Referenda In Cities and Counties

In cities and counties in which the public library is not a public library district but rather a department of municipal government, the library will need to work with the city council or county legislative body and get them to adopt a bond resolution approving your project and its financing. In a county, the adoption of this bond resolution will not usually be subject to permissive referendum and thus no mandatory referendum can be called on the legislative body's own motion. In a city, same story unless the city charter provides otherwise.

A "City and County Library" is a specially chartered entity with its own rules pursuant to Chapter 768 of the Laws of 1953, established by a county legislative body which is responsible for any capital projects, following usual county bond resolution adoption procedures.

Some cities may have special library districts (in which they are one of two joint Affiliated Entities in some cases) and these library districts are subject to the rules provided in their state establishment legislation. That special legislation will generally provide the how, what, when and where of any referendum requirement and process.

Referenda In Joint Public Libraries

A public library with more than one Affiliated Entity is usually the creation of a special act of the State Legislature. That legislation must be reviewed for the referendum requirements, if any, for a capital improvement project. In any case in which a public library has more than one Affiliated Entity and no special legislation, it is likely the result of a long-term contractual agreement between two political subdivisions (town, cities, counties, villages, school districts) and that contract should be consulted for the allocation and treatment of capital project financings.

Projects To Be Financed Through The Dormitory Authority

Special mention must be made with regard to projects that a Library District intends to finance or may finance, through the Dormitory Authority of the State of New York. Library District propositions for these projects must include certain specific language in addition to the basic proposition requirements. *See* Chapter 21 herein.

Library Improvements Without An Increase In The Tax Levy

If the vote in a Library District capital project referendum is, most fundamentally, upon an increase in the tax levy to cover debt service on the capital project, what are the rules if no tax increase is needed? While perhaps rare, some district public libraries are the beneficiaries of bequests, gifts, or special contracts with other educational institutions and they have or will have the cash needed to either (i) pay for the project outright or (ii) pay debt service on debt issued for the project without an increase to the tax levy. Must they nevertheless go to the voters for project approval?

While it is not free from doubt, an answer to this question is found in Opin. No. 76-771, 32 Opinions of the State Comptroller 105 (1976)(further supported in Opin No 79-474 (1979)), and that answer is simply, no, there is no need to go to the voters in such a circumstance, if the sole issue is whether to proceed with a capital project. The opinion is reproduced in Chapter 9 under the subheading "Mortgage Notes of a Library District," and involves a context of expenditure of surplus monies. The answer may be different if bonding is anticipated. It is important to note that such opinions are advisory and are not binding on the courts.

CHAPTER FIVE

After the Referendum Process

So, the voters said yes! Hallelujah! You are off to the races! Soliciting bids! Signing Contracts! Picking out the wallpaper for the bathrooms! STOP!

Listen, folks. The voters gave you the authority to do the project and to raise their taxes to pay debt service on bonds. Remember the bond part? Well, now, immediately after the vote, and *before* you sign the contracts and order the bookcases, you need the source of the funding for it all to be authorized. And for Library Districts, that takes the adoption of a bond resolution by the legislative body of your Affiliated Entity. *That* implements the will of the people to finance the project they approved.

Without a valid bond resolution, you are still without authority to contract for the work to be done if you intend to pay for the work through bonding (because you do not yet have a source of funds to pay for any contractual obligation).

Once the bond resolution is adopted and becomes effective, then it also serves as a statement of intent to borrow. Then, if necessary you have legal authority to advance moneys in anticipation of repaying yourself from an eventual borrowing.

CHAPTER SIX

Anatomy of a Bond Resolution and Its Adoption

In general, the State Legislature has, by the enactment of the Local Finance Law, authorized the power and procedure for each type of municipality and school district in the State to borrow and incur indebtedness, subject, of course, to the constraining Constitutional and statutory provisions set forth previously.

Once a proposal has been approved by the voters of a Library District, the Affiliated Entity must adopt a bond resolution to implement that vote. Once a municipality has decided to make a capital improvement for its own (non-district) library, that municipality must likewise adopt a bond resolution.

Bond Resolutions

Pursuant to the provisions of the Local Finance Law, school districts and municipalities authorize the issuance of bonds to finance a capital project, known as an "object or purpose" therein by the adoption of a bond resolution. Bond resolutions are usually drafted by specialized counsel known as bond counsel who will ultimately opine as to the validity of any debt issued thereunder as well as the tax-exempt status of its interest. A bond resolution is approved by a super-majority vote of two-thirds of the voting strength of the members of the legislative body of the Affiliated Entity acting as the finance board, in the case of a Library District, after a successful Library District referendum, to implement the vote. Voting strength means the total membership of the board, not simply those board members present at the meeting. Customarily, a finance board delegates to its chief fiscal officer, the power to authorize and sell bond anticipation notes in anticipation of authorized bonds, as well as the bonds themselves pursuant to Section 56.00 of the Local Finance Law.

The delegation of the power and duties to sell and issue debt to the chief fiscal officer does not remove the legislative body from the transaction completely: Sections 20.00 and 163.00 of the Local Finance Law provide that the chief fiscal officer must file a certificate with the legislative body upon sale and issuance providing all of the terms and conditions thereof. In addition, a legislative body holds the power to either limit the delegation of authority or elect to reassume the same pursuant to Section 56.00 of the Local Finance Law. This is rarely, if ever, utilized as the sale of debt is customarily subject to market conditions requiring very prompt action.

Once delegated to the chief fiscal officer, Section 160.10 of the Local Finance Law permits the chief fiscal officer to make a further written delegation to a deputy of any delegated powers.

Each bond resolution authorizes the construction, reconstruction, acquisition, or installation of an "object or purpose" to be financed, sets forth the plan of financing and specifies the maximum maturity of the bonds subject to the legal (Constitution, Local Finance Law and case law) restrictions relating to the period of probable usefulness with respect thereto. Typically, Library Districts have bonds authorized by their Affiliated Entity within the Constitutional constraints noted above for building construction, reconstruction and additions, acquisition of land, equipment, machinery and furnishings.

A school district or municipality may adopt one or more bond resolutions authorizing the issuance of bonds for a specific object or purpose, for which object or purpose serial bonds may be issued. In addition thereto, a school district or municipality may adopt one or more bond resolutions authorizing the issuance of bonds for any class of objects or purposes, for which objects or purposes serial bonds are to be issued. It basically must mirror what the Library District voters approved.

The issuance of obligations for a capital improvement and for the acquisition of land or permanent rights in land for such improvement may be authorized by the same bond resolution, notwithstanding the fact that the subdivision of paragraph a of section 11.00 of the Local Finance Law which sets forth the period of probable usefulness for such capital improvement (hereinafter described) does not include therein the acquisition of land or permanent rights in land for such improvement.

Proceeds of a borrowing pursuant to bond resolution may never be legally used for any other purpose than that described in the bond resolution. Once borrowed, no reallocation to some other purpose is permissible; the only permissible use of such borrowed proceeds, if not used for the project as described, is to pay down debt service on the debt obligation under which the money was borrowed.

The requisite elements to every bond resolution, discussed below, are based on the few basic Constitutional principles and limitations described previously.

Elements of a Bond Resolution

What does a bond resolution do? The function of any bond resolution is, in essence, to authorize the financing of a valid capital project. A bond resolution has several essential components:

a. **accurate description of the item(s) or improvement(s) to be financed. Here is a typical example:**

   Section 1. The reconstruction of the Jerry Garcia Memorial Public Library Building in the Haight Central School District, Ashbury County, New York, including original furnishings, equipment, machinery, apparatus, appurtenances and incidental improvements and expenses in connection therewith, is hereby authorized at a **maximum estimated cost** of $___________.

b. statement as to whether the item or improvement is a specific object or purpose or a class of objects or purposes. Here is a typical example:

Section 2. It is hereby determined that the plan for the financing of said specific object or purpose is as follows:

c. statement of maximum estimated cost of the project; the "hard costs" of a capital project may have added to them such "soft costs" as those for planning, public hearings, environmental impact review, title fees, interest during construction, and, yes, attorneys fees. Here is a typical example:

Section 1. The reconstruction of the Jerry Garcia Memorial Public Library Building in the Haight Central School District, Ashbury County, New York, including original furnishings, equipment, machinery, apparatus, appurtenances and incidental improvements and expenses in connection therewith, is hereby authorized at a **maximum estimated cost** of $____________.

d. plan of financing of the cost, i.e., how much to be financed, how much cash is to be used, if any, sources of cash contribution to estimated cost. Here is a typical example:

Section 2. It is hereby determined that the plan for the financing of said specific object or purpose is as follows:

(a) by the issuance of the $__________ serial bonds hereby authorized to be issued pursuant to the provisions of the Local Finance Law; and

(b) by the expenditure of $__________ building capital reserve fund moneys, which moneys are hereby appropriated therefor.

e. statement of the period of probable usefulness of the capital project and the maximum maturity of the bonds authorized. Here is a typical example:

Section 3. It is hereby determined that the period of probable usefulness of the aforesaid specific object or purpose is 25 years, pursuant to subdivision 12(a)(1) of paragraph a of Section 11.00 of the Local Finance Law. It is hereby further determined that the maximum maturity of the serial bonds herein authorized will exceed five years.

f. delegation of authority to the chief fiscal officer, to arrange for the financing by bonds and/or bond anticipation notes as well as renewals of said notes (this is not mandatory but is customary to permit prompt activity when needed). Here is a typical example:

Section 4. Subject to the provisions of the Local Finance Law, the power to authorize the issuance of and to sell bond anticipation notes in anticipation of the issuance and sale of the serial bonds herein authorized, including renewals of such notes, is hereby delegated to the Board President, the chief fiscal officer. Such notes shall be of such terms, form and contents, and shall be sold in such manner, as may be prescribed by said Board President, consistent with the provisions of the Local Finance Law.

Section 5. All other matters, except as provided herein relating to such bonds including determining whether to issue such bonds having substantially level or declining annual debt service and all matters related thereto, prescribing whether manual or facsimile signatures shall appear on said bonds, prescribing the method for the recording of ownership of said bonds, appointing the fiscal agent or agents for said bonds, providing for the printing and delivery of said bonds (and if said bonds are to be executed in the name of the School District by the facsimile signature of the Board President, providing for the manual countersignature of a fiscal agent or of a designated official of the School District), the date, denominations, maturities and interest payment dates, place or places of payment, and also including the consolidation with other issues, shall be determined by the Board President. It is hereby determined that it is to the financial advantage of the School District not to impose and collect from registered owners of such serial bonds any charges for mailing, shipping and insuring bonds transferred or exchanged by the fiscal agent, and, accordingly, pursuant to paragraph c of Section 70.00 of the Local Finance Law, no such charges shall be so collected by the fiscal agent. Such bonds shall contain substantially the recital of validity clause provided for in section 52.00 of the Local Finance Law and shall otherwise be in such form and contain such recitals in addition to those required by section 52.00 of the Local Finance Law, as the Board President shall determine.

Section 6. Such bonds shall be in fully registered form and shall be signed in the name of the Haight Central School District, Ashbury County, New York, by the manual or facsimile signature of the Board President and a facsimile of its corporate seal shall be imprinted or impressed thereon and may be attested by the manual or facsimile signature of the School District Clerk.

g. pledge of the full faith and credit of the School District to pay any such obligations by using its unlimited taxing power (the "general obligation" pledge). Here is a typical example:

Section 7. The faith and credit of said Haight Central School District, Ashbury County, New York, are hereby irrevocably pledged for the payment of the principal of and interest on such bonds as the same respectively become due and payable. An annual appropriation shall be made in each year sufficient to pay the principal of and interest on such bonds becoming due and payable in such year. There shall annually be levied on all the taxable real property of said School District a tax sufficient to pay the principal of and interest on such bonds as the same become due and payable.

h. a reimbursement authorization. Here is a typical example:

Section 8. This resolution shall constitute a statement of official intent for purposes of Treasury Regulations Section 1.150 - 2. Other than as specified in this resolution, no moneys are, or are reasonably expected to be, reserved, allocated on a long-term basis, or otherwise set aside with respect to the permanent funding of the object or purpose described herein.

i. an estoppel clause. Here is a typical example:

Section 9. The validity of such bonds and bond anticipation notes may be contested only if:

1) Such obligations are authorized for an object or purpose for which said School District is not authorized to expend money, or

2) The provisions of law which should be complied with at the date of publication of this resolution are not substantially complied with, and

an action, suit or proceeding contesting such validity is commenced within twenty days after the date of such publication, or

3) Such obligations are authorized in violation of the provisions of the Constitution,

and

j. a directive to the clerk to publish the estoppel notice described in Chapter Eight. Here is a typical example:

Section 10. This resolution, which takes effect immediately, shall be published in full in *The East Village Other* and *The Oracle*, the official newspapers of said School District, together with a notice of the School District Clerk in substantially the form provided in Section 81.00 of the Local Finance Law.

Temporary Advances of Non-Borrowed Moneys/Bond Resolutions for Planning

Temporary advances of other available moneys for a project prior to authorization of financing can be a problem.

Bond resolutions to authorize the financing of the cost of planning for a future capital improvement deserve special comment. While preliminary costs, such as the fees of architects, surveys, planners, and environmental analysis, may be rolled into and included in the authorization for borrowing of the capital improvement, there are times when the latter cost cannot be determined until some of the initial costs are incurred. Section 165.10 of the Local Finance Law does not permit reimbursement of those, or any costs, paid temporarily with other available funds, unless a valid bond resolution is in place at the time of expenditure. (There is a similar rule under federal tax law governing tax-exempt obligations - this is the reason for item "(h)" above) This dilemma is usually resolved in one of two ways: (a) adoption of a bond resolution with a somewhat high estimate of the ultimate total cost, including initial planning, or (b) adoption of a bond resolution just for the initial planning costs. There is, however, a trap for the unwary in adoption of a bond resolution only for planning costs. Section 99-d of the General Municipal Law provides that where a board has authorized debt issuance for planning costs, authorization for the undertaking of the actual improvement itself cannot occur during the one-year period after such debt is issued. Section 99-d of the General Municipal Law provides that where a board has authorized debt issuance for planning costs, authorization for the undertaking of the actual improvement itself cannot occur during the one year period thereafter. (Section 99-d also places a limit on the aggregate amount of stand-alone advance planning financings that can be authorized in any fiscal year. That ceiling is generally 5% of the "amount of the annual budget.")

The continued purpose for this rule is unclear in an era when construction projects typically move more quickly than that. Legislation could be introduced to eliminate this unnecessary restriction, which is observed more in the breach in any event.

If a bond resolution for planning costs is adopted, however, the period of probable usefulness for same is five years; however, upon adoption of the later bond resolution for the hard costs, and assuming five years have not elapsed, the period of probable usefulness of the planning can be extended to the full period of probable usefulness for the capital improvement in the later bond resolution. One consequence of this to note: the maximum maturity for debt issued for any aspect of the project, hard or soft, now is determined to have begun running from the first borrowing for planning, if borrowing occurred rather than a temporary advance of available moneys. This can be significant in large projects with extended planning periods if the period of probable usefulness, for example, of reconstruction of a building is twenty years, but planning financing was separately authorized, and utilized over a two-year period prior to construction, the cost of the building itself must now be paid off over eighteen years, rather than twenty, increasing the annual debt service burden on the taxpayers.

Since even a bond resolution for planning is subject to voter approval in a school district, this option is rarely, if ever, utilized in school districts. It is utilized in cities, towns, villages and counties.

In any case in which a Library District intends to reimburse itself from borrowed proceeds for moneys temporarily advanced for any aspect of a capital project, the adoption of a bond resolution by the Affiliated Entity is necessary prior to the advance under current law. Current law is modifiable by state legislative action. In the meantime, at a minimum, and with no guarantee that is adequate, a Library District expending moneys prior to a referendum for the initial stages of a capital project, should adopt a "resolution of intent to reimburse" to signal the clear intention of the Library Board of Trustees to reimburse temporary advance of cash upon approval of the project by the voters and, adoption of an implementing bond resolution.

Additional Money Bond Resolutions / Phased Projects

There are times when the bid cost of a capital project comes in higher than that authorized in the bond resolution. What to do? A special form of bond resolution known as an "additional money" bond resolution may be adopted if it is desired to finance the increased cost. This is subject to the same voting requirements in the same order as for the initial financing. Such a resolution does not amend the existing bond resolution (if moneys have already been borrowed under it);

rather, it supplements the existing bond resolution and the new plan of financing refers the prior bond resolution. It is subject to all the same rules as other bond resolutions and the PPU for the additional costs runs from the first borrowing under the existing bond resolution. Compare this with providing funding for phases of a single large capital project: some projects, generally large ones, have separate construction phases and it is possible to authorize the financing one phase at a time especially the cost of later phases, as they may be dependent on how the earlier phase(s) work out. Note that this method of authorization can put larger projects at risk mid-construction if later bond authorizations fail to get the requisite approval.

Bond Resolutions and Contingencies to Utilization

Bond resolutions generally cannot include contingencies to their utilization. (However, adoption of a bond resolution does not require that it ever be utilized in whole or in part.) Why? Because the lenders to an Affiliated Entity, and bond counsel, need surety that the bond resolution is valid. A built-in contingency would impinge on the certainty of valid adoption. In short, bond counsel could not opine in the required "unqualified opinion" that the debt was valid without following up on a contingency and obtaining certified satisfaction that the contingency was met. Reasonable people could differ as to whether the contingency had, in fact, been met. Hence, contingencies are not found in bond resolutions. The only exception to this rule is that pertaining to grants and loans and the determination not to borrow long term to the extent such funds are received.

Repeal of a Bond Resolution

Section 41.00 of the Local Finance Law governs the repeal of all or a portion of a bond resolution.

In relevant part for a school district, for example, this reads:

"§41.00 Repeal of unexpended authorizations

a. The finance board of:

2. Any school district may at any time, by resolution, repeal or revoke in whole or in part (a) any resolution heretofore or hereafter adopted authorizing the issuance of obligations, at any time after four years have elapsed from the date of adoption of any such resolution and (b) any certificate of a chief fiscal officer authorizing the issuance of obligations, dated on or after the effective date of this chapter at any time after four years have elapsed from the date of any such certificate. . . except to the extent that any indebtedness shall already have been contracted or encumbrances made thereunder for the object or purpose for which such resolution or certificate authorizes the issuance of obligations . . . .

b. Any resolution heretofore or hereafter adopted authorizing the issuance of obligations, or any certificate of a chief fiscal officer authorizing the issuance of obligations, dated on or after the effective date of this chapter, unless repealed or revoked at a prior date in the manner provided in paragraph a of this section, shall be deemed to be repealed ten years after the date it becomes effective, except to the extent that any indebtedness shall already have been contracted or encumbrances made thereunder for the object or purpose for which such resolution or certificate authorizes the issuance of obligations."

This latter provision is to ensure that such unexpended authorizations will not unnecessarily swell the “authorized but unissued indebtedness” disclosure in an official statement and other filings.

CHAPTER SEVEN

Certain Legal Elements of a Financed Capital Project

Periods of Probable Usefulness

Every capital project to be financeable must have a legally set period of probable usefulness ("PPU") which establishes a maximum maturity date for any debt issued for that project. Paragraph a of Section 11.00 of the Local Finance Law assigns periods of probable usefulness to those improvements and other objects or purposes that the State Legislature has determined can have a PPU; without a PPU set forth in this section (or otherwise, in for example, special legislation), a project is not considered capital and therefore no capital debt can be issued for such projects. As Section 10.00 of the LFL states:

> "**§ 10.00 Power of municipalities, school districts and district corporations to contract indebtedness.**
>
> . . . a municipality, school district or district corporation shall have the power to contract indebtedness respectively for any municipal, school district or district corporation object or purpose set forth in paragraph a of section 11.00 of this title, or for a class of such objects or purposes when authorized under the provisions of section 31.00 of this article, if it is authorized by law to expend money for or to accomplish such object or purpose; provided, however, that it shall not be able to contract indebtedness to a greater extent than it is authorized by law to spend money for such object or purpose or class of such objects or purposes and provided also that this section shall not relieve any such unit of government of any duty imposed by law to include in its annual budget or tax levy or otherwise to pay from current funds all or part of any expenditure that it may make for such object or purpose or class of such objects or purposes."

Typical periods of probable usefulness are, for example, five (5) years for buses, five (5), ten (10) or fifteen (15) years for various items of public works or maintenance type equipment (depending on cost), twenty to thirty years for building construction, expansion or reconstruction, depending on the materials utilized, thirty years for land acquisition, and forty years for water and sewer projects. The legislative body of the Affiliated Entity may prescribe a serial bond maturity period for any number of years equal to or less than the PPU (but never greater than the legally prescribed PPU). The PPU establishes the maximum maturity for any borrowing or series of borrowings for a project; it does not mandate that the maximum be utilized (but it does provide the greatest flexibility over time). A board is always able to limit the maximum maturity in the bond resolution or a borrower is always able to voluntarily implement the payoff of its debt over a shorter period, if preferable. It is also true that there is not generally a public market for local governmental debt that has a final maturity beyond the 25–30 year range.

The maximum maturity date of any borrowing or series of borrowings for a single capital project is thus set with the initial borrowing for that project because it is from that date that the period of probable usefulness is calculated. If, for example, a school district borrows on behalf of a Library District to construct a new library building with a PPU of twenty-five years by issuance of a one-year bond anticipation note ("BAN") to obtain funds during construction, and then, the following year, refinances that BAN with a serial bond issue, the final maturity of that bond issue cannot exceed twenty-four (24) years, taking into account that there has already been debt (the BAN) outstanding for one year. Likewise, on a larger, multi-year project, multiple new money borrowings during construction (commonly known as "series") all have the running of their maximum maturity tied to the date of the very first borrowing. Each series is not entitled to the full PPU as if it were the first borrowing—rather the first borrowing has already established the longest maturity date for any debt issued for that particular capital project. (Needless to say, however, a related but different capital project, which is not additional, increased costs of the same project, would have its own full PPU.)

Specific Object or Purpose or Classes of Objects or Purposes

A bond resolution can authorize a specific object(s) or purpose(s) or a class (or classes) of objects or purposes. If the legislative body, for example, specifies an exact number of items it plans to acquire, that is "specific" and the cost of each particular item is specific and must be specified; if it authorizes the acquisition of "computers," that is a "class" with a single aggregate cost. What is the difference? If a specific number of items is authorized, that is what must acquired each at no more than the specified cost; if it turns out the amount of dollars authorized is insufficient for any particular item, this is a problem. Even if the aggregate authorization would cover the insufficiency for that item, there is no authority to move authorization from one item that turned out to be less costly to one that turned out to be more costly. If, however, a class is authorized, i.e., "acquisition of computers," then greater flexibility ensues. Some flexibility is generally preferable for just this reason. While such problems are rare, they can be quite embarrassing. Issues can particularly arise, in bond resolutions for multi-facility building projects when the cost of work at one building comes in high while another comes in lower than expected. There is thus an art to the drafting of bond resolutions.

The LFL provides this guidance of definitions of "specific" and "class":

> "The term "specific" as applied to the terms "object or purpose," "capital improvement" or "equipment" shall mean a single item, or a specified number of items, the description of which is contained in a single subdivision of paragraph a of section 11.00 of this chapter."

"The term "class," as applied to the terms "objects or purposes," "capital improvements' or "equipment," shall mean an unspecified number of items, the description of which is contained in a single subdivision, other than subdivision thirty-five of paragraph a of section 11.00 of this chapter, notwithstanding the fact that such subdivision may be drafted in the singular number."

and then permits either to be used in drafting a bond resolution:

"Any municipality, school district or district corporation may adopt one or more bond resolutions . . . authorizing the issuance of bonds . . . for a special object or purpose, for which object or purpose serial bonds may be issued. In addition thereto any municipality or school district may adopt one or more bond resolutions . . . authorizing the issuance of bonds . . . for any class of objects or purposes, for which objects or purposes serial bonds may be issued."

Policing a Class of Objects or Purposes

One may well ask, if a capital project is described generally, as a class of objects or purposes; i.e. reconstruction of Library District buildings, how can one know which particular facilities under consideration before the Board of Trustees at the time of the referendum are those intended to receive the funding (and therefore required to receive the funding)? The answer is actually quite simple: the record of adoption by the Board of Trustees includes the written materials relating to the financing as well as the record of debate at adoption. These form the "legislative history" of the bond resolution adoption and provide the roadmap to legislative intent as to the use of the borrowed proceeds.

In the case of grant aided projects within a class, by the terms of the grant they are usually the only legal recipients of the aid portion of the cost of that project.

A chief fiscal officer, in any event, has no power to increase or decrease appropriation or enter into contract beyond the scope of authority. That power is vested only in the legislative board. No delegation of this power is permissible.

Further Aggregation of Items

In addition to the determination of whether a capital project is a specific object or purpose or a class of objects or purposes, it may also be possible for a legislative body to aggregate multiple *related* capital projects under one of the "super-PPUs" established by the State Legislature for projects with a common PPU of 5, 10, 15, 20, 25, 30, 35, or 40 years. This is most useful in circumstances in which the exact costs of certain related components of a capital program are not known at the time of adoption of the bond resolution. If the dollar cost of each component is not yet known, these components of a library district program can possibly share a common PPU as long as it does not exceed the maximum permitted PPU of any one of the components, i.e. if one element of a capital project has a 15-year PPU and a second element has a 10-year PPU, a combined 10-year PPU (the lowest common denominator) could be used for the aggregated costs of both.

A typical context for use of a super-PPU is the acquisition of a parcel of land and the building thereon. Land has a 30-year PPU and a building acquisition can have a 30-year PPU if it is a fireproof building. Neither the seller nor the library district may know a reasonable allocation of the cost of the purchase price to the land and to the building—since they both have in 30-year PPU, it may be possible to combine them in one aggregate cost.

While there is some uncertainty about the proper use of super-PPUs, they are in use throughout the State, at least in the case of *related* improvements for bond resolutions not subject to permissive or mandatory referendum. Arguably, this modality could not be used in a school district but school districts have been provided a special super-PPU for state-aided building projects only (See below).

Section 32.00 (4) provides that a bond resolution includes:

> "4. A determination of the period or periods of probable usefulness of the specific object or purpose or class of objects or purposes for which such bonds . . . are to be issued, if such determination is made by the finance board. However, if bonds are to be used for a class of objects or purposes for which more than one period of probable usefulness is prescribed pursuant to section 11.00 of this chapter and if the determination of the period of probable usefulness therefore is to be made by the finance board, the bond resolution authorizing the issuance of such bonds shall
>
> > "(a) Specify the kind of specific object or purpose within such class to which the proceeds of such bonds are to be applied and the appropriate period of probable usefulness therefore, or
> >
> > "(b) Specify as the period of probable usefulness of such class the lowest period of probable usefulness assigned thereto."

This is the basis for the super-PPUs.

Special Super Period of Probable Usefulness for School Districts

As part of the revision of state building aid in Chapter 383 of the Laws of 2001, the State Legislature provided a new super-PPU for school district building projects which are aidable.

As part of Section 11.00 of the Local Finance Law, it reads as follows:

> "Educational facilities. The acquisition, construction, reconstruction, improvement, rehabilitation, repair, furnishing or equipping of a school construction project eligible for the apportionment of aid pursuant to subdivision six of section thirty-six of the education law, thirty years."

This super-PPU is only available for facilities which receive that particular aid and thus library district projects may not generally qualify (state building aid being such a byzantine universe we wouldn't hazard a guess what qualifies). Thus, this super-PPU is now in common use for school district capital building and rebuilding projects across the state. It certainly simplifies both the text of bond resolutions and the language of bond propositions (which incidentally must be consistent). One question raised by the language of subdivision 97 of Section 11.00 of the Local Finance Law is: Does it intend to bundle ineligible costs as well in the 30 year useful life? Reasonable people may differ but from a practical point of view, it would be politically inexpedient and factually perhaps be impossible to bifurcate a capital project into eligible and ineligible parts each with their own cost prior to a referendum and adoption of a bond resolution. This is one reason why school district bond resolutions always utilize the estoppel procedure described in Chapter 8 hereof.

Maximum Estimated Cost

The maximum estimated cost of a capital project stated in a bond resolution is intended to be just that and nothing more or less. It is self-evident that how the scope of a project is described will expand or limit its maximum estimated cost. For example, a capital project with multiple sources of funds, only one of which is the local share, could be described in one of two ways:

a. To pay the Library District's share of the cost of construction of a new parking lot at the Icabod Crane Memorial Library Building (the "Local Share Model" or "net funding")
b. To pay the cost of construction of a new Library District parking lot at the Icabod Crane Memorial Library Building (the "Full Cost Model" or "gross funding").

The Local Share Model focuses on the local share only. Thus it does not allow for a school district or municipality to "gross fund" a capital project with federal and/or state grants-in-aid, i.e. temporarily borrow on short-term bond anticipation notes (but not bonds) until the grant moneys arrive. Since many grants require a temporary local advance of the grant portion, as well as truly local share, this Local Share Model of the bond resolution would not work in those cases. A Full Cost Model of bond resolution will state the total maximum estimated cost and then provide in the plan of financing (described below) for the various sources of funding. As such it can include (or not) borrowing authority for the grant portion and that borrowing authority can be limited to bond anticipation notes. This proviso looks like this in a bond resolution:

> Section 2. It is hereby determined that the plan for the financing of the aforesaid specific object or purpose is by the issuance of $4,459,150 serial bonds of said School District hereby authorized to be issued therefor pursuant to the provisions of the Local Finance Law; **PROVIDED, HOWEVER,** that to the extent that any Federal or State grants-in-aid are received for such specific object or purpose, the amount of bonds to be issued pursuant to this resolution shall be reduced dollar for dollar.

In as much as a Library District proposition must authorize the full maximum estimated cost and authorize anticipated maximum annual debt service in the budget for as long as debt is outstanding; it only makes sense to follow the gross funding model in the case of Library District Projects.

Keep in mind that a maximum estimated cost for a plan of financing is a maximum ESTIMATED cost. As provided in Section 32.00 (2) of the LFL:

> ". . . Such financial plan, by virtue of its inclusion in such resolution, shall not be deemed binding upon such municipality, school district or district corporation."

In other words, the maximum estimated cost may change at some point after adoption of the bond resolution. That will require amendment of some capital plan and project authorization proceedings, and it may require amendments or supplementation of the bond resolution. Note: The additional costs, financed or not, may well mean in cases in which the initial cost was subject to referendum that the whole election process must be revisited in order for the voters to approve the project at the increased cost (regardless of the source of funding of same.) Furthermore, reduced costs which will result in reduced borrowings do not require amendment of a bond resolution, but repeal of unused authorizations is recommended periodically.

Plan of Financing

As discussed above, the scope of a capital project can be described in a bond resolution as the local share or the entire cost. In either event, a bond resolution must contain a plan of financing paragraph that sets forth the source(s) of funding for the capital project as described. Again, Section 32.00 (2) of the LFL clarifies that changes to the plan do not require amendment or supplementation of a bond resolution unless there are additional costs to be financed. In such circumstances, a bond resolution to cover specifically the additional costs is the recommended course. Such an additional money bond resolution references the prior bond resolution in the plan of finance and with regard to the beginning date for calculating the maximum maturity under the shared PPU.

Some Peculiar PPU Rules

Some peculiar rules in the Local Finance Law about certain financeable and non-financeable items:

1. There is no PPU for books even though the British Museum, the British Library, the Library of Congress and other repositories have a few rather old ones around suggesting that they do last, as capital items should.
2. The useful life of new buildings depends on what they are made of.
3. The useful life for building reconstruction/additions depends on what it is made of.
4. Road resurfacing has a different useful life than parking lot resurfacing.
5. Repairs are not financeable but reconstruction is.
6. Replacing a general telephone system, including Web-based telephone, has no specific PPU, but a "911" system or a police or fire telephone system does. (A general 5 year equipment subdivision may be used.)
7. HVAC and electrical, plumbing and lighting work has one useful life if done as a stand-alone project and a longer useful life if it is part of or involves "reconstruction."
8. Land has useful life of 30 years. (What happens to it after that?)
9. There is a PPU for underground fuel tanks but not for above-ground fuel tanks. Not very green.

10. If you can get an “expert” to certify as to the useful life of something not listed in Section 11.00 of the LFL, it is financeable for that period of time (or less).
11. A capital project with a PPU can include incidental expenses. What is “incidental” may be in the eye of the beholder, but it should be reasonable. (Really!)
12. Computer equipment for financial management and accounting has its own PPUs for hardware and software but no other computer equipment has a specified useful life (must use generic equipment category for it).

Some of this seem illogical? It is. Bottom Line: PPUs are an art, not a science, but it is not worth it to push the limits.

CHAPTER EIGHT

Estoppel

The LFL provides that where a bond resolution is published with a statutory form of estoppel notice, and the bond resolution itself contains an estoppel provision, the validity of the bonds authorized thereby, including bond anticipation notes issued in anticipation of the sale thereof, may be contested only if:

a. such obligations are authorized for a purpose for which the local governmental unit is not authorized to expend money; or
b. there has not been substantial compliance with the provisions of law which should have been complied with in the authorization of such obligations; or
c. an action, suit, or proceeding contesting such validity, is commenced within twenty days after the date of such publication; or
d. such obligations are authorized in violation of the provisions of the State Constitution.

Except on rare occasions most local governmental units comply with this estoppel procedure. It is a procedure that is recommended by bond counsel, but it is not an absolute legal requirement.

In any case, after adoption of a bond resolution, a legal notice of estoppel should be published.

What is estoppel and why publish the notice?

If a bond resolution authorizing the issuance of bonds and BANs contains the estoppel statement referred to in section 80.00 of the LFL, such resolution after adoption, or a summary of such resolution, should be published in full by the school district or municipal clerk of the Affiliated Entity, together with a notice in substantially the following form:

> "The resolution (or the resolution a summary of which is) published herewith has been adopted on the ______ day of ________________, 20___, and the validity of the obligations authorized by such resolution may be hereafter contested only if such obligations were authorized for an object or purpose for which the (Here insert name of school district or municipality) is not authorized to expend money or if the provisions of law that should have been complied with as of the date of publication of this notice

were not substantially complied with, and an action, suit or proceeding contesting such validity is commenced within twenty days after the date of publication of this notice, or such obligations were authorized in violation of the provisions of the Constitution."

[name]
(school district or municipal clerk)

In the past a legal notice of estoppel always contained both the estoppel statement noted above plus the full text of the bond resolution. Due to rising publication costs, it is now customary to publish a summary legal notice of estoppel which includes the estoppel statement, the bond resolution title, a very brief description of the specific object or purpose or class of objects or purposes (i.e., the capital project), the maximum estimated cost of same, the plan of financing of same, including how much cash, and how many bonds, and the period of probable usefulness, as well as an indication as to where the full text may be examined. The use of a summary form of this notice is authorized in Section 81.00 of the LFL.

If a summary of such resolution is published, such summary must list the specific or class or classes of objects or purposes for which the obligations to be authorized by such resolution are to be issued together with the period or periods of probable usefulness, SEQRA status, and the amount of obligations to be issued for each such specific or class of objects or purposes, and in addition, such summary must state an office of the school district or municipality where the resolution summarized thereby is to be available for public inspection. Such resolution must be kept available for public inspection at such office during normal business hours for twenty days following the publication of such summary.

Such publication is to be in the official newspaper or newspapers of the school district or municipality which is the Affiliated Entity, or if there be no such newspaper or newspapers, then in such newspaper or newspapers having a general circulation in the school district or municipality as their governing board shall designate (usually within the text of the bond resolution).

Timing. There is no timing requirement as to how quickly an estoppel notice must be published after adoption of a bond resolution which is effective immediately. Any time after adoption of the implementing bond resolution after the referendum it is permissible to publish the notice. While it is legal to contract for a project during the estoppel period, it is generally not recommended until the twenty-day estoppel period has elapsed. Why? Because estoppel protects the issuer and its debt obligations from any validity challenge, other than on constitutional grounds once the twenty-day period after publication has elapsed. Thus, any procedural error inadvertently occurring in the process of authorization may not be used to challenge the borrowing after estoppel has passed. The twenty (20) day estoppel period begins to run on the date of publication. Thus, the sooner it is able to be published, the better. The estoppel notice is usually drafted by bond counsel.

If the obligations issued pursuant to a resolution published in the manner described above contain a recital in substantially the form prescribed in Section 52.00 of the LFL, such recital binds the Affiliated Entity issuing such obligations, and twenty (20) days after such resolution has been published and after such obligations have been purchased in good faith and for fair value by any person, the validity of such obligations cannot be questioned by such Affiliated Entity or any taxpayer thereof in any court (unless the Affiliated Entity has violated a provision of the State Constitution). Thus, the library district, the issuer and the purchaser are protected by estoppel.

CHAPTER NINE

Types of Debt

The LFL authorizes a variety of types of debt instruments for school districts and municipalities, all of which must be general obligations, which pledge the faith and credit of the issuer to the payment of the indebtedness. Debt instruments which are not specifically authorized include, for example, a revolving line of credit at a local bank, a revenue bond backed not by the pledge of the faith and credit, but rather solely backed by some particular stream of revenue, or a bond with a security interest in a building or other asset. A library needs to know which type of debt obligations its Affiliated Entity can issue and the rules governing such debt. (Note that these are the rules applicable to the Affiliated Entity. The Library District (or a free association library) itself may enter into a mortgage note financing which a school district or municipality cannot as noted in Chapter 2 and the subsection of this chapter entitled "Mortgage Notes of a Library District." Mortgage notes of a Library District are *not* LFL debt.)

The basic types of debt instruments most frequently utilized in the State by school districts and municipalities are as follows:

a. bond anticipation notes ("BANs") and bond anticipation renewal notes ("BARNs");
b. serial bonds;
c. statutory installment bonds;
d. tax anticipation notes ("TANs");
e. revenue anticipation notes ("RANs");
f. budget notes;

Less common are:

g. specialized bond types, including capital appreciation bonds, original issue discount bonds, variable rate bonds, term bonds and joint indebtedness;
h. capital notes; and
i. refunding bonds.

Each of these are described later in this chapter. Even less common are:

j. urban renewal notes

k. deferred payment notes
l. land installment purchase obligations (until July 31, 2011)
m. deficiency notes (first authorized by Chapter 386 of the Laws of 2010 to finance a deficiency in any fund arising from a revenue shortfall during a fiscal year).

These latter four categories are not discussed herein.

The basic elements of any type of bond or note are to be found in Sections 51.00 and 52.00 of the LFL, which read as follows:

§51.00 Terms, form and contents of obligations

Every bond and note shall contain a statement of at least the following:

1. The type of obligation
2. The amount of the obligation and the total amount of the issue of which the obligation is a part.
3. The date and maturity of the obligation.
4. If the obligation is a tax anticipation note or a revenue anticipation note, the fiscal year for which the taxes were levied or are to be levied or in which the revenues are to become due and payable, as the case may be; if the obligation is a tax anticipation note to be issued in anticipation of the levy or collection of assessments for a fiscal year or in anticipation of the collection of an installment of an assessment for a capital improvement, the fiscal year for which such assessments were levied or are to be levied or in which such installment becomes due, as the case may be.
5. The rate of interest or, in the case of obligations bearing a variable rate of interest, the procedure for calculating such variable rate of interest and the maximum rate of interest which such variable rate notes may bear, together with the date or dates of payment thereof. [Eff. Until July 15, 2012]
6. The rate of interest and the date or dates of payment thereof. [Eff. July 15, 2012]
7. The place or places of payment of principal and interest.
8. The medium of payment.
9. An irrevocable pledge of the faith and credit of the municipality, school district or district corporation issuing the obligation for payment thereof.
10. If the obligation is payable to bearer, whether it may be converted into a registered obligation; if the obligation is in registered form, whether it may be converted into a bearer obligation.
11. If the obligation may be called for redemption prior to its date of maturity, the terms and conditions under which such obligation may be redeemed.

and:

§52.00 Recital of validity in obligations

Any obligation issued by a municipality, school district or district corporation may contain on its face a recital in substantially the following form:

"It is hereby certified and recited that all conditions, acts and things required by the Constitution and statutes of the State of New York to exist, to have happened and to have been performed precedent to and in the issuance of this (*Here insert type of obligation*), exist, have happened and have been performed, and that the issue of (*Here insert type of obligations*) of which this is one, together with all other indebtedness of such (*Here insert name of municipality, school district or district corporation*) is within every debt and other limit prescribed by the Constitution and laws of such State.

The method of execution of any note is found in Section 61.00 of the LFL which reads:

§61.00 Execution of obligations

a. All obligations, including interim bonds, shall be executed in the name of the municipality, school district or district corporation by the chief fiscal officer unless the finance board shall by resolution, designate a different officer or officers to execute such obligations. Such execution may be by facsimile signature, in which event the finance board shall provide for authentication of such obligation by the manual countersignature of a fiscal agent or of a designated official of the municipality, school district or district corporation. Such obligations shall have the seal or a facsimile seal of the municipality, school district or district corporation impressed or imprinted thereon. Such obligations may be attested by the school district or district corporation or such other official thereof as may be designated by the finance board. Coupons attached to a bond shall be authenticated by the facsimile or manual signature of the chief fiscal officer unless the finance board shall, by resolution, provide that such coupons shall be authenticated by the facsimile or manual signature of a different officer.

b. Obligations executed in the manner set forth above by the officials designated and referred to above shall be valid and binding obligations when duly delivered, notwithstanding the fact that before the delivery thereof the persons executing the same shall have ceased to be officials or other officials may have been designated to perform such functions.

BANs and BARNs

BANs and BARNs are typically one (1) year or less, single fixed rate debt obligations, renewable annually at maturity at then current interest rates. Principal and interest are due at maturity. A new money borrowing is known as a BAN; its annual renewal is known as a BARN. BANs and BARNs are issued only for capital projects, never for cashflow purposes and never for a greater amount than the amount of bonds authorized for the capital project. However, a BAN may be issued for capital costs which include a portion of a project for which a grant is later anticipated. Once the grant is received, it usually must be used to pay down an equal portion of BAN principal at the next renewal date. It is often wise to authorize borrowing for both the local share and the non-local share of a project by BANs in case grant-in-aid moneys are delayed in receipt. Financing for all Library District projects must convert from BARNs to bonds no later than the fifth anniversary date after the first BAN. (If new money for a project was borrowed in series, each series must comply with the 5-year rule independently and is not tied, for this purpose, to the very first new money borrowing.) (Also, there is an exception to this general rule for assessable improvements in, for example, Town improvement districts)

While BANs and their renewals may be authorized by one, or annual, BAN/BARN resolutions, it is far more common that the original bond resolution authorizing the issuance of serial bonds for the capital project, includes a delegation of authority to the Board President as chief fiscal officer to issue BANs and BARNs as well as the eventual bonds. Which method is used is a political, rather than legal, decision. Flexibility and quick action ensue from full delegation so it is common nowadays when markets can change quite rapidly.

One final feature of BANs and BARNs is worthy of note: either may be issued for less than one year or with an early redemption feature which would permit the optional right (of the issuer) to call in and pay off such a note prior to its maturity date. This option may be useful when a Library District plans to convert notes issued on its behalf to bonds sometime during the forthcoming fiscal year but is for any number of factors unsure precisely when. Similarly, either BANs or BARNs can be issued for over one year, up to five years, as long as provision is made for specific annual principal paydowns in the documents.

Serial Bonds

Serial bonds are the most common long-term debt obligations issued by school districts and municipalities in the State. They are often referred to as "plain vanilla general obligation bonds;" "plain vanilla" meaning they are a simple form of debt instrument with multiple succeeding annual maturities of principal, each maturity of which has a single fixed rate of interest. The "general obligation" aspect refers to the constitutionally required pledge of the faith and credit of the school district or municipality to use its taxing power to pay the debt, no matter what.

Serial bonds may be issued either (a) to redeem outstanding BANs and/or BARNs, or (b) to acquire new money to pay the cost of all or a portion of one or more capital projects. A combination of these purposes is also permitted. Bonds issued to finance all or a portion of the cost of multiple capital projects, and/or to refinance the same, are known as consolidated bond issues. There is no restriction on how many projects may be consolidated for purposes of sale into a single bond issue. (The same is true of BANs and BARNs.) However, each project in such a consolidation must maintain a separate accounting for purposes of its annual requisite principal paydown schedule, its PPU and its maximum maturity. Only in the case of debt sold with a substantially level or declining annual debt service structure may these elements be merged, aggregated and averaged across all the individual capital projects financed in a consolidated serial bond issue.

Serial bonds mature serially; that is, one after the other in their stated principal amounts, annually on the same day each year until final maturity. That annual maturity day can be any date but the first or the fifteenth of any calendar month are most common. Principal must be paid annually and by custom interest is paid semiannually in most serial bond issues. Serial bonds may carry an early redemption feature—the industry custom is 10-year call protection; that is, the first ten (10) years of a serial bond issue are not "callable," i.e., redeemable prior to maturity. (There is some experimentation lately with call features in the 5–7 year range.) Early redemption usually involves payment of a small premium to the bondholder at the time of the call (almost always in the 2% of principal redeemed early or less range, depending on how soon prior to stated maturity the call occurs). In the current low interest rate environment, a par call (without premium) is common. This feature is set at the time of sale of serial bonds in consultation with a financial advisor and bond counsel.

One exception to the requirement that annual principal be paid is the basic 2-year rule applicable at the beginning of a borrowing cycle for a project, which comes into play here: The first payment of principal on a new money borrowing (by series) need not be paid until the second anniversary of the first borrowing. This initial one-year optional moratorium period on payment of principal may occur during the period of time that the financing for a project is still in its BAN/BARN cycle or, it may occur within the structuring of the serial bond issue. The two years runs from the first borrowing (by series) for a capital project regardless of the form that borrowing has taken. Each new money borrowing starts operation of its own 2-year rule; therefore, in multiple new money borrowings over time for a single project, each such series has its own timetable in this regard.

In plain English, this means that an Affiliated Entity, and thus the Library District must make a principal payment within two years of the date of issuance of a borrowing of new money (i.e., not renewals; once a borrowing reaches the 2 year mark, annual principal paydowns are required thereafter at each renewal).

By omission, then, the statute permits one to make no payment at the end of the first year and, for example, roll over a bond anticipation note in full (or skip that first principal payment in a new money bond issue).

As an example, take a $100,000 financing with a 10-year maturity. The municipality issues $100,000 bond anticipation note in year one. At the end of year one, the municipality makes a $10,000 principal payment and issues a $90,000 renewal note. At the end of year two (the year in which a principal payment is mandated by the statute) the municipality makes a $5,000 principal payment. This is an automatic violation of the 50% rule, because the 50% rule says that no principal payment may exceed by more than 50% the smallest previous principal payment mandated by law. By making the principal payment in the amount of $5,000, no subsequent payment may legally exceed $7,500, and one can see that over the next eight years, it is impossible to amortize the remaining $85,000 without violating the 50% rule.

Consider a different scenario, however: at the end of the first year, the municipality makes a $5,000 principal payment. The uninitiated would conclude, using the reasoning above, that there is an automatic violation of the 50% rule. This is not correct. After all, the LFL provides that no principal payment need be made at the end of year one. If that is the case, then why should a municipality be punished for making a "voluntary" payment at the end of year one. Thus, for the purpose of the 50% rule, one can disregard the first payment in this case, since it was voluntary, not mandated by law.

Serial bonds for multiple capital projects each contain pro-rata allocations of principal relating to the different projects financed by the bond issue. In each maturity, there will be multiple projects represented to the extent that each such project has not exceeded its maximum maturity. Thus in the first five years after issuance, all consolidated projects may be amortizing but in the sixth year, any project with a five-year PPU will have already been paid off in full in the prior annual maturity (except in the case of substantially level or declining annual debt service which merges all project PPUs to a shared average, as described earlier). It is part of the function of a financial advisor and bond counsel to ensure compliance of the whole and its parts to these rules.

In a consolidated serial bond issue, each component must be in compliance with the 50% rule described earlier, or be part of a substantially level or declining annual debt service amortization structure which has aggregated all components.

At each maturity of a serial bond issue, a portion of the principal due on each consolidated project is and must be annually paid down (no skipping of principal paydowns is permitted after the initial year), together with semiannual interest due on all outstanding maturities. On the other semiannual interest payment date, just interest due on all outstanding serial bonds is due. Therefore, note, the interest due on any interest payment date always relates to multiple outstanding maturities, not just the particular maturity amount of principal due in that particular year. There is only one rate of interest per maturity—these aggregate for the overall debt service payment due at such semiannual date.

How is principal and interest paid when due on outstanding bonds or notes? An Affiliated Entity can pay a bank or trust company located and authorized to do business in the State to act as fiscal agent for the debt. Those duties and responsibilities are set forth in Section 70.00 of the LFL. In brief, they are payment of debt service when due, conversion, re-conversion and transfer of bonds and notes, preparation of substitute bonds and notes for lost or destroyed ones, and related services.

Alternatively, an officer of the Affiliated Entity may serve as the fiscal agent. This is common in this era of book-entry-only issued debt (described below). Unless otherwise named, the particular officer is specified in Section 70.00 of the LFL. It is the job of the fiscal agent to wire the principal and interest when due to the holders of the debt obligations. Nowadays, with the prevalence of book-entry-only debt, it is usually only necessary to wire payment to one party, a national repository holding the debt on behalf of all owners. It is then their responsibility to forward the funds to the beneficial owners. *See* "DTC" in the "Transaction Players and Their Roles" appendix herein.

Finally, serial bonds may only be issued for valid capital projects, each specified in Section 11.00 of the LFL and identified as a specific object or purpose or a class of objects or purposes. They may not be issued for cashflow purposes, including the redemption of outstanding RANs, TANs or budget notes (further described below). Through special legislation, however, bonds to finance the payoff of a cumulative budgetary deficit can be given a period of probable usefulness, declared as a valid object or purpose and be issued.

To summarize, consistent with rules discussed earlier, the first payment of principal in a serial bond issue must also conform to the following rules:

a. it must occur within two years of the date of issuance of all new money or for any such portion;
b. it must occur annually thereafter;

c. it must occur no later than the fifth anniversary date of any first borrowing for a non-assessable project included in the bond issue that was previously financed with BANs and BARNs; and
d. it must be paid, like each succeeding principal payment, by an annual appropriation.

To further summarize, consistent with the above rules, the last payment of principal in a serial bond issue must conform to the following rules:

a. it must occur on a date no later than the maximum maturity date calculated based upon the PPU of each of the projects or average PPUs of the projects, and the first borrowing date(s) for each project or each series of new money borrowings for a project;
b. it must occur no later than the expiration of the period of probable usefulness of the object or purpose (or average objects or purposes in the case of level annual debt service) for which the serial bonds were issued as computed from the date of such bonds, or if BANs and BARNs were issued in anticipation of the bonds, as computed from the date of the earlier note so issued;
c. it must not exceed by more than 50% any prior principal payment on a project-by-project basis internal to the maturity or, if the bonds were issued with substantially level or declining annual debt service, it must not exceed by more than 5% or $10,000, whichever is greater, any prior annual debt service for the bond issue as a whole.

When serial bonds are issued, traditionally there were multiple printed bonds issued for each maturity adding up to the total per maturity in paper form, each with the owner's name (or, in prehistory, "Bearer"), the amount, the maturity date, (or, actual interest "coupons") the interest rate, and the interest payment date schedule on it. Nowadays, most bonds are issued in book-entry-only form such that only one printed bond is issued for each annual maturity and held at a national repository on behalf of all owners, whose ownership record is maintained electronically. *See* "DTC" in the "Transactional Players and Their Roles" appendix hereto. The basic elements of a serial bond are provided in Sections 51.00 and 52.00 of the LFL as noted earlier and the rules of their execution are found in Section 61.00 thereof, as provided above. It is a function of bond counsel to prepare the actual physical, printed bonds (and notes) for issuance by a school district or municipality.

Statutory Installment Bonds

Statutory Installment Bonds ("SIBs") are a somewhat simplified type of serial bond. All of the rules of amortization described above apply; however, instead of printed bonds for each maturity, an SIB is a single "typewritten" style bond representing all maturities which, in addition to regular serial bond information described above, also includes a full principal amortization schedule and separate interest payment schedule (SIBs are the form of serial bonds in which one occasionally sees annual rather than semiannual interest payments). If the principal amount for an object or purpose, or objects or purposes, or class or classes thereof, to be financed by the issuance of bonds does not exceed one million dollars ($1,000,000; $5,000,000 until June 1, 2012 under a temporary expansion of authority granted in Chapter 386 of the Laws of 2010) in the aggregate, a single SIB may be issued for the full principal amount. No issuer may issue over one million dollars in SIBs in a fiscal year. Any such bond shall provide for the payment of both the principal and interest upon physical presentation of the bond for notation of such payments thereon (except SIBs issued and sold to the United States of America or any agency thereof in any amount may have principal and interest payable without such presentation). The notations of principal and interest payments are to be made on the face of the bond, on the reverse side, or on a sheet attached thereto.

SIBs can be issued for new money purposes or to refinance a BAN or BARN or both. Since SIBs may not exceed one million dollars ($1,000,000; $5,000,000 until June 1, 2012) in principal and require physical notation, they are typically placed with local banks in the community where the issuer is located (and deposits its fund balances). While capital projects of any period of probable usefulness and maximum maturity may be financed with an SIB, local banks typically do not like to invest in SIBs with maturities greater than ten (10) years. This forms a market-based maximum maturity limitation on projects with longer than ten year PPUs. It is not uncommon for school districts to issue SIBs to finance their school bus replacement program or small capital reconstruction projects.

SIBs are usually sold at private sale rather than public sale. This distinction is discussed below in Chapter 11.

There is a standard form to an SIB which is provided in detail in Section 62.10 of the LFL.

§62.10 Statutory installment bonds

a. Notwithstanding any other provisions of this chapter, if the principal amount for an object or purpose, or objects or purposes, or class or classes thereof, to be financed by the issuance of bonds does not exceed one million dollars in the aggregate, a single bond, to be known as a statutory installment bond, may be issued for the full principal amount, if the issue is to be sold at private sale. Any such bond shall provide for the payment of both the principal and interest upon presentation of the bond for notation of such payments thereon, except that such a statutory installment bond may be issued and sold to the United States of America or any agency thereof in any amount and that such principal and interest shall be payable without such presentation.

b. A statutory installment bond, in bearer, if authorized by federal law, or registered form, shall be in terms, form and contents, substantially as follows:

Statutory	United State of America	$ (*Here insert full*
Installment	State of New York	*amount of bond issue*)
Bond	School District of	
	(*Here insert name of the issuer*)	

(*Here insert type of bond and year, such as "Library Bookmobile Serial Bond—2010"*)

The (*Here insert name of the issuer*), in the school district of ___________________, a (*Here insert whether a municipality, school district, fire district or other district corporation*) of the State of New York, hereby acknowledges itself indebted and for value received promises to pay to (*Here insert "bearer" or the name of registered owner if the bond is issued in registered form*) the principal sum of ________ Dollars ($_______ (in (______) equal annual installments of _______ Dollars ($_____) on the _______ day of ________ in the years, 20__, to 20__, inclusive)

Or

(in _________ (_________) annual installments (*Here state the amounts, the annual principal payment date, and the year in which the principal payments will be made. No annual installment shall be more than fifty percent in excess of the smallest prior installment unless the finance board has determined to provide for substantially level or declining annual debt service, in which case the aggregate amount of debt service payable in any year shall not exceed the lowest aggregate amount of debt service payable in any prior year by more than five percent*))

and to pay interest on the unpaid balance of such principal sum at the rate of _____________ per centum (_____%) per annum, semiannually on the _________ days of __________ and ___________ in each year from the date of this bond until it matures. Interest will not be paid on any installment or principal, or of interest, after the due date thereof. Both the installments of principal of and the interest on this bond will be paid to the (*Here insert "bearer" or "registered owner" if the bond is issued in registered form*) of this bond in lawful money of the United States* only upon presentation of this bond for notation of any such payment thereon* (*omit language enclosed within asterisks when the bond is sold to the United States of America or any agency thereof*) at the office of ______________

(*Here insert place or places of payment*)

This bond is a statutory installment bond, the principal sum of which cannot exceed One/Five Million Dollars ($1,000,000/$5,000,000) unless it is issued and sold to the United States of America or any agency thereof, and is issued pursuant to section 62.10 of the Local Finance Law and pursuant to a bond resolution entitled "(*Here insert title*)," duly adopted by (*Here insert name of the finance board*) of such (*Here insert name of issuer*) on the _______ day of ___________, 20__. This bond may not be converted into a coupon bond.

The faith and credit of such (*Here insert name of the issuer*) are hereby irrevocably pledged for the punctual payment of the installments of principal of and the interest on this bond according to its terms.

It is hereby certified and recited that all conditions, acts and things required by the Constitution and statutes of the State of New York to exist, to have happened and to have been performed precedent to and in the issuance of this bond, exist, have happened and have been performed, and that this bond, together with all other indebtedness of such (*Here insert name of the issuer*) is within every debt and other limit prescribed by the Constitution and laws of such State.

In Witness Whereof, the (*Here insert name of the issuer*) has caused this bond to be signed by its (*Here insert title of officer*) and its (*Here insert title of officer*), and its corporate seal to be hereunto affixed and attested by its (*Here insert title of attesting officer*) and to be dated as of the _______ day of _______________, 20__.

(Corporate Seal) (*Name of municipality, school district, fire district or other district corporation*)
By: (*Signature and title of officer*)
and (*Signature and title of officer*)

Attest:
(*Signature and title of attesting officer*)

PRINCIPAL PAYMENT

Amount	Date Received	Received by
$____________	___________, 20__	___________________ (*Signature of person receiving payment*)
$____________	___________, 20__	___________________

(*Continue as necessary*)

INTEREST PAYMENT

Amount	Date Received	Received by
$____________	___________, 20__	___________________ (*Signature of person receiving payment*)
$____________	___________, 20__	___________________

(*Continue as necessary*)

The notations of principal and interest payments may be made on the face of the bond, on the reverse side, or on a sheet attached thereto (omit language enclosed within asterisks when the bond is sold to the United States of America or an agency thereof).

Note that until September 30, 2011, statutory installment bonds, in substantially the form noted above, may be issued and sold to the New York state environmental facilities corporation in a principal amount not to exceed twenty million dollars ($20,000,000) and such bonds can provide for either a fixed rate or, if such bonds provide for serial maturities, at a set rate, for each maturity, which rate is fixed on the date of issuance of such bonds. This provision is rather unlikely to be utilized by library districts.

BANs or Bonds for a Capital Project

There is an option to issue bonds or bond anticipation notes initially for a capital project. BANs generally mature within one year, at which time they may be renewed, after the paydown of a portion of the principal due (principal paydowns to begin no later than the second anniversary of the first borrowing). Similar to a variable rate home mortgage in respect to interest rate risk, each year at renewal, the issuer is subject to the then current interest rate environment and the issuer's then current rating by companies like Moody's who rate issuers. Nevertheless, as typically one year obligations, the interest rate is always, or almost always historically, lower than longer term debt. Thus, one might choose to issue one year BANs at the then current one year rate each year for five years. This option would also permit a Library District to use unexpected excess cash to pay down extra principal on any annual maturity date, prior to renewal.

The issuance of serial bonds to obtain funds for a capital project involves establishing at sale a single-interest rate or rates per maturity on a single date of sale, which then locks that rate or rates in for the life of the bonds. Likewise, the annual principal paydowns must be predetermined prior to sale in order to establish what the purchasers are going to be buying. There is usually no ability to pre-pay all or any portion of a serial bond issue within the first ten years after issuance. On the other hand, in a period of rising interest rates, it is a very reasonable decision to set and lock rates before they increase.

A typical borrowing pattern for construction or reconstruction projects involves issuing BANs and BARNs during construction and converting to serial bond financing after the project is complete. While this pattern is often followed to be sure all of the proceeds are in fact needed for the project, no Library District project has ever used less than the maximum amount authorized!

In addition to debt issued for a capital project, school districts and municipalities often issue short-term debt to keep their general fund solvent. A Library District may request that its Affiliated Entity issue same on its behalf.

Tax Anticipation Notes

Tax Anticipation Notes ("TANs") are a debt instrument issued for cashflow purposes. They are typically issued because the receipt of property taxes by a school district or municipality is not congruent with its cashflow expenditure requirements within its fiscal year cycle. TANs are not subject to the same amortization rules as debt issued for capital purposes. We will focus here on school district TANS but the rules are similar for other local units of government. A library district can request a school district to issue TANS on its behalf and according to Opinion 92-28 of the Office of the State Comptroller, the interest expense is that of the school district unless the Library District chooses to reimburse them.

TANs may be issued by any school district,

a. During a fiscal year in anticipation of the collection of taxes or assessments levied, or to be levied, for such fiscal year,
b. Within ten days prior to the commencement of a fiscal year or, where the fiscal year of the issuer is a calendar year, within thirty days prior to the commencement of a fiscal year, in anticipation of the collection of taxes or assessments levied, or to be levied, for such fiscal year,
c. During any fiscal year in anticipation of the collection of taxes or assessments levied for any of the four preceding fiscal years.

In the case of such notes issued in anticipation of the collection of taxes already levied, such notes may not be issued in an amount in excess of the amount of taxes levied for a fiscal year which is uncollected at the time of such borrowing (i.e., at closing, not at the date of sale of the TAN) less:

a. The amount of the outstanding tax anticipation notes issued in anticipation of the collection of such taxes, and
b. The amount, if any, included in the annual budget for such fiscal year or in the levy of taxes for such fiscal year to offset, in whole or in part, an anticipated deficiency in the collection before the end of such fiscal year of the taxes levied for such fiscal year.

In addition, there are federal tax regulations establishing limitations on the size of cashflow borrowings based upon a reasonably expected cashflow deficit during the term of the TAN and allowing for a small margin of comfort. *See* Chapter 12 for a further discussion of these tax considerations.

TANs must mature within one year from the date of their issuance and may be renewed from time to time, but each renewal may be for a period not to exceed one year. Such notes or the renewals thereof must be retired within five years after their date of original issue and in any event not later than five years after the close of the fiscal year for which were levied the taxes in anticipation of the collection of which such notes were issued; (however, such notes issued in anticipation of taxes to be levied (i.e., not yet levied at the time of borrowing), or the renewals thereof, may not extend beyond the close of the fourth fiscal year succeeding that in which the original notes were issued). TAN principal and interest is payable in a single payment (not semiannually) at maturity.

There are five other significant aspects to the issuance of TANs:

a. The authority to issue TANs is by resolution by the affirmative vote of the majority of the voting strength of the Board of Education; the TAN resolution typically delegates to the Board President as chief fiscal officer the authority to sell and issue TANs, often up to a capped amount and often only for a single fiscal year (but multi-year authorizations and delegations are permitted). There is no public referendum requirement. There is no estoppel or other public notice publication requirement after adoption. The essential elements of a TAN note are provided in Section 51.00 of the

LFL as discussed earlier. The essential elements of a TAN resolution are described in Section 39.00 of the LFL hereinafter set forth.

b. The proceeds of such notes are only to be used for the purposes for which the taxes or assessments in anticipation of which they are issued were or are to be levied or for the redemption of notes in renewal of which they were issued.

c. Whenever the amount of TANs issued in anticipation of the collection of the taxes or assessments levied or to be levied for a fiscal year equals the amount of such taxes or assessments remaining uncollected (less the amount, if any, included in the annual budget for such fiscal year or in the levy of taxes or assessments for such fiscal year to offset, in whole or in part, an anticipated deficiency in said collection before the end of such fiscal year), such moneys as thereafter collected, must be set aside in a special bank account to be used only for the payment of such notes as they become due, unless other provisions are made pursuant to law for the redemption of such notes. This is the LFL Section 24.00(e) debt service fund, also discussed later in this primer under tax considerations. Any School District may make budgetary appropriations for the redemption of such notes whether or not required or otherwise authorized by law to do so. In the event such an appropriation is made, such School District shall not be required to pay into the special account the proceeds of the taxes or assessments against which such notes were issued but such proceeds may be used in the manner provided by law or if there is no provision of law pertaining to the use of such proceeds, such proceeds shall be treated as surplus moneys for the fiscal year in which they are collected.

d. Where a tax anticipation note is to be renewed by the issuance of a renewal note, and the taxes or assessments in anticipation of which it was issued have been levied for a fiscal year, but remain uncollected, such renewal note shall not be issued for an amount in excess of the amount of such taxes or assessments remaining uncollected at the time of such renewal, less:

   (a) The amount of any other outstanding tax anticipation notes issued in anticipation of the collection of such taxes or assessments, and

   (b) The amount, if any, included in the annual budget for such fiscal year or in the levy of taxes or assessments for such fiscal year to offset, in whole or in part, an anticipated deficiency in the collection before the end of such fiscal year of the taxes or assessments levied for such fiscal year.

   Renewal notes cannot be issued for an amount in excess of the amount of the note in renewal of which it is to be issued, including TANs issued in anticipation of taxes or assessments which remain unlevied as of the renewal date.

e. There are other specialized rules in Section 24.00 of the LFL for issuing TANs in special circumstances such as prior to the adoption of an annual budget.

Revenue Anticipation Notes

Revenue anticipation notes ("RANs") are a second common debt instrument issued for cashflow purposes by school districts. Again, RANs are typically issued because the receipt of some particular form of revenue, e.g., state aid to school districts, is not congruent with cashflow expenditure requirements within the fiscal year cycle. Like TANs, RANs are not subject to the same amortization rules as debt for capital projects. We will again focus on school districts but other local government units have similar treatment. It is likely that a library district could request a school district to issue RANs on its behalf but there are technical issues which would need to be considered.

RANs may only be issued in anticipation of receipt of certain types of revenues and then, only such revenues due and payable within the fiscal year of issuance. The common types of revenue against which RANs may be issued are taxes other than real estate taxes (i.e., sales tax), rents, rates or charges (such as special fee revenues, and grant-in-aid moneys from the State or Federal government, tuition payments to special act school districts). Because of the pay back limitations described below, it is usually preferable to borrow in anticipation of grants-in-aid for capital projects through BANs which can be renewed up to 5 years while awaiting such grant receipt.

RANs may be issued by any school district in anticipation of the collection or receipt of revenue, provided that each such note shall be issued only against a specific type of revenue, or for the purpose of renewing a previously issued RAN. A RAN may be issued in anticipation of multiple types of revenues, but in such case each such type must be separately accounted for in authorizing documentation and for purposes of all applicable rules.

RANs may be issued during any fiscal year in which such taxes, rents, rates or charges or other income in anticipation of which such notes are issued become due and payable or such moneys become due; however, such notes may be issued by a school district in anticipation of moneys to be received in a fiscal year during the two weeks prior to the commencement of such fiscal year.

The total amount of RANs which a school district may issue in anticipation of the collection or receipt of a specific type of revenue is to be determined in the following manner:

1. In a typical school district in which an annual budget is prepared and adopted for a fiscal year prior to the commencement thereof, such amounts must be:
   a. The amount of such specific type of revenue as estimated in the annual budget of such municipality, school district or district corporation for such fiscal year, or the amount of such specific type of revenue recognized for the fiscal year preceding that for which such budget is to be or has been adopted, whichever amount is the smaller, less
   b. The amount of such specific type of revenue so estimated in each budget which has actually be received or collected at the time of the issuance (not sale) of such RANs, and the amount of any outstanding RANs issued against such specific type or revenue for the fiscal year for which such notes are to be issued.

> These provisions are not applicable (1) where a specific type of revenue has not been estimated in such budget and in that case such amount may be the amount of such revenue as is estimated by the chief fiscal officer to be recognized for the fiscal year for which such budget has been adopted, or (2) where a specific type of revenue has not been recognized for the entire fiscal year preceding that for which such budget has been adopted and in that case such amount may be the amount, if any, of the specific type of revenue as estimated in the annual budget, less, in either case, the amount of such specific type of revenue which has actually been received or collected at the time of the issuance of such notes, and the amount of any outstanding RANs issued against such specific type of revenue for the fiscal year for which such notes are to be issued.

In addition to this limitation under the LFL, there are applicable federal tax regulations limiting sizing as noted in the discussion of TANs. *See* Chapter 12.

There are three other significant aspects to the issuance of RANs:

a. The authority to issue RANs is typically by resolution by the affirmative vote of the majority of the voting strength of the Board of Education. The RAN resolution typically delegates to the chief fiscal officer the authority to sell and issue RANs, often up to a capped amount and often only for a single fiscal year (but multiyear authorizations and delegations are permitted). There is no public referendum requirement. There is no estoppel or other public notice publication requirement after adoption. The essential elements of a RAN resolution, like a TAN resolution, are described in Section 39.00 of the LFL hereinafter discussed. The essential elements of a RAN note, like a TAN note, are provided in Section 51.00 of the LFL.
b. Whenever the amount of RANs issued for a fiscal year against a specific type of revenue shall be the estimated amount of such specific type of revenue in anticipation of the collection or receipt of which such notes shall have been issued, less the amount of such revenue actually received or collected, all of such revenue, as thereafter received or collected, is to be set aside in a special bank account to be used only for the payment of such revenue anticipation notes as they become due. This is the LFL Section 25.00(g) debt service fund also discussed later in this primer under tax considerations. Any school district may make budgetary appropriations for the redemption of revenue anticipation notes whether or not required or otherwise authorized by law to do so. In the event such an appropriation is made, such school district is not required to pay into the special account of proceeds of the specific type of revenue against which such notes were issued but such proceeds may be used in the manner provided by law or if there is no provision of law pertaining to the use of such proceeds, such proceeds shall be treated as surplus moneys for the fiscal year in which they are collected.

c. RANs must mature within one year and may be renewed from time to time, but each renewal must be for a period not exceeding one year and in no event may such notes, or the renewals thereof, extend beyond the close of the second fiscal year succeeding the fiscal year in which such notes were issued. Such notes may not be renewed in an amount in excess of the difference between the amount of the uncollected or unreceived revenue in anticipation of which they were issued and the amount of any other outstanding revenue anticipation notes issued in anticipation of the collection or receipt of such revenue. RAN principal and interest is payable solely at maturity.

TAN and RAN Resolutions Format

The following provision of law governs the text of both TAN and RAN resolutions.

§39.00 Tax anticipation note resolution, revenue anticipation note resolution and urban renewal note resolution, form and contents.

a. Whenever the finance board shall authorize the issuance of tax anticipation notes, revenue anticipation notes or urban renewal notes, or the renewal of such notes, it shall do so by a "tax anticipation note resolution," a "revenue anticipation note resolution" or an "urban renewal note resolution," as the case may be. Each such resolution shall be properly dated and shall bear a title which will indicate the type of note to which it relates. Whenever any such note has been duly authorized by a chief fiscal officer the certificate required to be filed by such officer pursuant to section 30.00 of this chapter shall bear a title which will indicate the type of note to which it relates.

b. A tax anticipation note resolution, revenue anticipation note resolution or an urban renewal note resolution shall contain, in substance, the following provisions:

1. A statement that such notes are issued in anticipation of:

(a) The tax collection of real estate taxes or assessments, in the case of tax anticipation notes;

(b) The collection of revenues other than real estate taxes or assessments, in the case of revenue anticipation notes; or

(c) The receipt of moneys from (1) the sale of real property, or any interest therein, acquired for or incidental to an urban renewal project; or (2) from the United States government pursuant to title one of the federal housing act of nineteen hundred forty-nine, as amended; or (3) from the state of New York pursuant to the general municipal law; or from any or all such sources, in the case of urban renewal notes.

2. (a) In the case of tax anticipation notes:

(1) If such taxes or assessments were levied or are to be levied for a fiscal year, a statement of the fiscal year for which such taxes or assessments were levied or are to be levied, or

(2) If such notes are to be issued in anticipation of the collection of assessments levied for a capital improvement and to be collected in a single installment, and, if such assessments have been levied, a statement of the date of the levy of such assessments, or

(3) If such notes are to be issued in anticipation of the collection of an installment of assessment which are levied for a capital improvement and which are to be collected in

several installments, and, if such installment of assessments has been levied, a statement of the date on which such installment is due and payable.

3. (a) In the case of revenue anticipation notes, a statement of the assessments have been levied, a statement of the amount of such taxes or assessments remaining uncollected against which such notes are authorized to be issued.

   (b) In the case of revenue anticipation notes, a statement of the amount of uncollected revenues against which such notes are authorized to be issued.

   (c) In the case of urban renewal notes, a statement of (1) the total estimated cost of the urban renewal project as stated in the certificate of the chief fiscal officer of the municipality filed and approved in the manner prescribed in paragraph d of section 25.10 of this chapter; (2) the total amount of any and all advances, loans and grants made by the United States government or by the state of New York in aid of such project to the municipality prior to and including the date of the issuance of any such note or notes; (3) the amount of any and all local grants-in-aid made or to be made for such project; and (4) the total amount of such notes outstanding for such project.

4. In the case of urban renewal notes, a statement identifying the particular urban renewal project with respect to which such notes are to be issued.

5. A statement of the amount of such notes to be issued.

6. A statement of the period of maturity on such notes.

7. (a) In the case of tax anticipation notes issued in anticipation of the collection of taxes or assessments which have been levied, or the renewals thereof, a statement that the date of maturity of such notes shall not extend beyond the close of the applicable period provided in section 24.00 of this chapter for the maturity of such notes.

   (b) In the case of revenue anticipation notes, if such notes are to be issued in renewal of similar notes, a statement that the date of maturity of such notes shall not extend beyond the expiration of the second fiscal year succeeding the fiscal year in which such original notes were issued.

Budget Notes

Various local units of government may issue budget notes. Again, we focus on school districts but the rules are similar for other political subdivisions. While there is no authority for a Library District to itself issue a budget note, it might be possible for an Affiliated Entity to do so although budget notes are said to relate to the specific budget of the issuing political subdivision. This question may require an opinion of the Office of the State Comptroller.

A school district may issue budget notes only during the last nine months of any fiscal year for expenditures for which an insufficient or no provision is made in the annual budget for such fiscal year. The amount may not exceed five per cent of such annual budget (unless the budget note resolution is approved by a majority of the qualified voters of the school district present and voting at any annual or special meeting of the school district held pursuant to the provisions of the Education Law during the last nine months of such fiscal year). The limitation is not applicable in cases of unforeseen public emergency.

Budget notes must be redeemed out of the taxes or assessments levied or to be levied for the fiscal year in which they mature or out of other revenues of that fiscal year legally available for that purpose. Principal and interest is payable solely at maturity.

Any school district or municipality which has the power to issue budget notes is also granted the power to appropriate and expend money received from the proceeds of the sale of budget notes for the purposes for which such notes are issued.

There are also special rules for budget notes for certain insurance purposes, snow and ice removal, judgments and settled claims; and other specific problematic budgetary situations.

It is important to note that, while budget notes may be issued due to increased expenses or to cover costs of unforeseen public emergencies, there is no authority to issue budget notes for revenue shortfalls of any kind. That is considered a problem to be solved by cost-cutting, cashflow borrowings, midyear tax or fee increases and/or deficit financing.

Budget notes are authorized by a budget note resolution of the legislative body by the affirmative vote of a majority of the voting strength. A public referendum is not required. Delegation to the chief fiscal officer of sale and issuance duties is common. There is no publication requirement. The essential elements of a budget note resolution may be found in Section 40.00 of the LFL, as follows:

§40.00 Budget note resolution; form and contents; authorization thereof

a. The issuance of budget notes or renewals thereof shall be authorized by a "budget note resolution." Each such resolution shall be properly dated and shall bear a title which will indicate that it relates to a budget note.

b. Any municipality, school district or district corporation may adopt one or more budget note resolutions authorizing the issuance of budget notes for a specific object or purpose, for which object or purpose budget notes may be issued. In addition, any municipality may adopt one or more budget note resolutions authorizing the issuance of budget notes for a class of objects or purposes set forth in paragraph b, c, d or e of section 29.00 of this chapter.

c. A budget note resolution shall contain, in substance, at least the following provisions:

1. A statement setting forth the facts and circumstances necessitating the issuance of such budget notes and the specific object or purpose or the class of objects or purposes for which the budget notes to be authorized by such resolution are to be issued and stating that there are no other funds available with which to pay or provide for such object or purpose or class of objects or purposes. Such circumstances necessitating the issuance of budget notes and such specific object or purpose shall be described in brief and general terms sufficient for a reasonable identification.
2. A statement of the amount of budget notes to be issued for such specific object or purpose or class of objects or purposes.
3. A statement of the period of maturity of such notes.

4. If such notes are to be issued in renewal of other notes a statement that the date of maturity of such notes shall not extend beyond the applicable period provided in section 29.00 of this chapter for the maturity of such notes.

d. Every budget note resolution shall be adopted by at least a majority vote of the voting strength of the finance board. A majority vote shall be sufficient for the adoption of a resolution authorizing the renewal of any budget note.

The essential elements of a budget note are also provided in Section 51.00 of the LFL, as described earlier.

The issuance of a budget note is a red flag to the rating agencies that there are fiscal problems at the issuer and should be avoided if at all possible.

Specialized Bond Types

In addition to the plain vanilla fixed rate general obligation serial bonds, some local governmental units in the State have authority to issue certain specialized type long-term debt obligations, including capital appreciation bonds ("CABs"), and original issue discount ("OID") bonds, including zero coupon bonds, variable rate bonds, and term bonds (otherwise known as sinking fund bonds). While each of these bond types must be issued as general obligation bonds, they each include features as to the nature or timing of interest or as to partial mandatory redemption of principal by lot that appeal to certain types of investors in certain markets. These instruments are very rarely issued in the State. It is only important to note their available authority and the need to put separate provisions in a bond resolution, or, if necessary, amending resolutions to permit the use of them. Investment banking firms will make issuers, their local counsel, their bond counsel and their financial advisors aware when such instruments might be an advantageous form of issuance, because such debt can be sold on a negotiated basis to them.

Capital Notes

In the hoary days of antiquity when dinosaurs still roamed the State, the authorization for the financing of most capital projects by most types of municipalities, required a five percent so called "down payment" to be appropriated in cash as part of the financing plan. This was considered to be "earnest money"—the local governmental unit really had to want the capital project enough to use some currently raised taxpayer dollars. For many years, prior to 1991, when this requirement was eliminated, a municipality could also satisfy this requirement, however, through the issuance of capital notes. (This effectively negated the "earnest money" aspect of the down payment.)

Nowadays, capital notes are rarely issued. While it is still permissible to authorize the financing of a capital project in whole or in part with capital notes instead of BANs and bonds, the particular requirements for principal payoff are not appealing: such capital notes may be renewed from time to time but such notes, including the renewals thereof, must mature not later than the first day of the second fiscal year succeeding the fiscal year in which such notes are issued. In addition, an installment of not less than fifty per cent of the principal amount of such notes must mature in the first fiscal year succeeding the fiscal year in which such notes are issued, unless such notes are authorized and issued during a fiscal year at a time subsequent to the date of the adoption of the annual budget for the next succeeding fiscal year. (In such case, one more year is permissible.) As a result, BANs and BARNs are much more common due to their flexibility and longer term renewability.

Capital notes must be redeemed out of taxes or assessments levied or to be levied for the fiscal year in which they mature or other legally available revenues of that fiscal year. They cannot be automatically converted to BARNs, but can be refinanced with bonds. Principal and interest are payable at maturity.

Capital notes and capital renewal notes are each authorized by adoption of a capital note resolution adopted by the legislative body by an affirmative vote of two-thirds of the voting strength. Unlike bond anticipation notes and bond anticipation renewal notes, the renewal of a capital note cannot be authorized and delegated in the original capital note resolution. The essential elements of a capital note or capital renewal note resolution may be found in Section 32.00 of the LFL, and are the same as for a bond resolution, discussed elsewhere herein. The essential elements of a capital note are provided in Section 51.00 of the LFL, as described earlier.

Refunding Bonds

What is an advance refunding? An advance refunding is a refinancing of outstanding bonds by the issuance of new bonds. It is thus not unlike refinancing a home mortgage note. It is a transaction in which a school district or municipality issues new bonds ("refunding bonds"), the proceeds of which are placed in an escrow account (in a bank or trust company located and licensed to do business in New York State). The proceeds, after payment of costs of issuance, are used to purchase special United States Treasury securities (generally directly from the Bureau of the Public Debt Division of the U.S. Treasury Department), the principal and interest payments of which are then used to pay the outstanding, now "refunded bonds." Debt service on the refunded bonds is paid from those investment proceeds in the escrow account. The refunded bonds are subsequently (on their "call date") "called" for early redemption prior to their stated maturity date, if such bonds have such a call feature. Many plain vanilla general obligation bonds have such a call feature available as of and after the date ten years from the original dated date of the bonds.

Certain outstanding bonds without a call feature rarely may be refunded in advance, but in such a case, the escrow account is established to pay debt service on the refunded bonds to each bond maturity date rather than an earlier "call date."

It is generally necessary to issue a greater amount of refunding bonds than the amount of bonds to be refunded due to two factors:

a. The costs of issuance of the refunding bonds (which may be included in the refunding bond size rather than paid in cash). These costs include: bond counsel, financial advisor, escrow agent bank, independent verification agent (to confirm that the escrow is sufficient to pay off the outstanding bonds), local counsel, and underwriter's fees.

b. The amount of money necessary to invest in U.S. Treasury securities to pay off the outstanding bonds (which are generally at a higher interest rate(s)) is necessarily more than the outstanding, refunded bond amounts because the escrow will pay principal *and* interest on the refunded debt and will be invested usually at a lower interest rate than the rate(s) on the refunded bonds (due, in part, to federal arbitrage rules governing advance refundings).

Present Value Savings. "Present value savings" is the historical benchmark requirement for advance refunding transactions in New York State: it is a time-value analysis of the stream of debt service payments due on the outstanding bonds in comparison to the proposed advance refunding bonds. The main governing provision of law, LFL Section 90.10, requires that there be present value savings for an advance refunding transaction to receive the legally-requisite approval of the Office of the State Comptroller (except certain Village transactions relating to state aid realignment. See Chapter Fourteen herein). Such transactions are generally not done unless the present value savings in dollars equal or exceed 3% of the outstanding principal amount of bonds to be refunded (although this 3% threshold is not a legal requirement). Thus, although a refunding bond may be larger in size than the remaining outstanding, refunded debt, the transaction *must*, nevertheless, make financial sense to proceed.

In addition, in order to receive the requisite approval of the State Comptroller, there are certain additional requirements.

Costs of Issuance of Refunding Bonds. The State Comptroller also must approve the full terms and conditions of the refunding transaction. What does this mean? It means that all of the fees and expenses of the transaction are subject to State Comptroller review prior to closing an advance refunding transaction. Section 90.10 of the LFL provides for the inclusion of such costs of issuance in the sizing of the refunding bond issue (thus automatically taking such bond-paid costs into account in any calculation of the present value savings of the transaction). Advance refunding transactions are the most complicated general obligation bond issues which a local governmental unit could undertake. There are more parties to the transaction, more documentation and more governmental oversight and approval than a "plain vanilla" capital project borrowing. As a result, advance refundings are more costly to complete. These costs should be taken into account in determining whether to proceed with such transactions. Consultation with a financial advisor is recommended on this point.

Board Action. Advance refunding transactions require adoption of a refunding bond resolution which includes a "preliminary refunding financial plan" (obtained from a willing underwriter/investment banking firm who will usually bring the refunding opportunity to the original issuer's attention in the first place). This is a specialized form of bond resolution with "magic" language known only to bond counsel. Some of it truly is essential to validity.

Voter Referendum. A voter referendum is generally *not* required with regard to doing an advance refunding transaction, despite the increased size of the refunding bond issue.

Steps in an Advance Refunding Transaction

a. Adoption of a Refunding Bond Resolution by affirmative vote of two-thirds of the voting strength of the governing board including an appendix with "Preliminary Refunding Financial Plan."

b. Publication of Legal Notice of Estoppel of Refunding Bond Resolution, or summary thereof.

c. After passage of minimum of twenty days, sale of Refunding Bonds can commence including, in the interim, preparation of Preliminary Official Statement and solicitation of bids for escrow bank and verification agent by financial advisor.

d. Sale of Refunding Bonds including initial advance purchase of special U.S. Treasury Securities of the State and Local Government Series ("SLGs") to fund escrow on closing date.

e. Application of Office of the State Comptroller for approval of transaction in accordance with requirements of Section 90.10 of the LFL. (Minimum 10 day approval period)

f. Closing of Refunding Bond Issue and purchase of SLGs to fund escrow.

g. The Escrow Account pays all refunded bond debt service when due until called and then the cost of redemption on the date all the bonds are called. The school district or municipality is responsible for debt service on the Refunding Bonds.

Qualified Zone Academy Bonds (QZABs)

General. Federal tax legislation enacted in 1997 and renewed in 2009 for issuances until 2011 (the "QZAB Law") authorized a debt instrument known as a "qualified zone academy bond" ("QZAB"). As described further below, this provision of the Internal Revenue Code of 1986 provides a source of funding that may be used for renovating school buildings, purchasing equipment, developing curricula and/or training school personnel. The proceeds of the QZABs may not be used for new construction. (A new type of tax credit bond, Qualified School Construction Bonds, was created by the American Recovery and Reinvestment Act of 2009 but will not be discussed here. Authorization is presently set to expire at the end of 2010.)

The QZAB program is a tax credit program. A QZAB provides an annual federal income tax credit to eligible taxpayers, who buy a QZAB, which include certain banks, insurance companies and other organizations actively engaged in the business of lending. The credit is deemed paid once a year and an eligible taxpayer may use it to offset its income tax liability for the taxable year in which the credit is received. Thus, QZABs reduce the burden of interest payments by giving certain financial institutions holding the QZABs a tax credit in lieu of interest. The school district must pay back the principal amount it initially borrowed, but it does not have to pay any interest (unless a supplemental interest payment is needed to sell the debt). The credit rate for QZABs sold on a given day is set by the United States Treasury Department.

Allocation. Prior to issuing a QZAB, a school district must receive allocation from the New York State Department of Education. The Department of Education administers the QZAB program through its School Facilities Planning Division. While it would appear that a school district could issue a QZAB to renovate its own school library, the provision does not seem to be applicable to Library Districts. Information is included here in the interest of completeness.

Qualifications. To be eligible to use a QZAB, at least 95% of the proceeds must be used for a "qualified purpose" with respect to a "qualified zone academy" established by a local education agency, i.e. Board of Education. The eligibility criteria are generally applied on a school-by-school basis, not district wide.

Qualified Purpose. A "qualified purpose" with respect to any qualified zone academy means (i) rehabilitating or repairing the public school facility in which the academy is established, (ii) providing equipment for use at such academy, (iii) developing course materials for education to be provided at such academy, and (vi) training teachers and other such personnel in such academy. The school district must prepare a written spending plan specifying how the proceeds of the QZAB are to be used.

Any school district applying for allocation to the New York State Department of Education under the QZAB Law should contact bond counsel during the application process to discuss possible finance structures to ensure that all items in the school district's application may be financed under New York law, and that any proposed sale method and amortization structure works under the LFL.

Qualified Zone Academy. So, what is a "qualified zone academy"? A "qualified zone academy" includes any public school or academic program within a public school (below the post-secondary level) if:

i. such school or program is designed in cooperation with business to enhance the academic curriculum, increase graduation and employment rates, or better prepare students for the rigors of college and the work force, and the school or program receives a private business contribution that is not less than 10% of the net present value of the proceeds of the QZAB;
ii. the comprehensive education plan of such school or program is approved by the governing school district and the students in such school or program are subject to the same academic standards and assessments as other students; and
iii. either the school is located in an empowerment zone or enterprise community or there is a reasonable expectation as of the date of issuance of the bonds that at least 35% of the students attending such school or participating in such program will be eligible for free or reduced cost lunches under the federal lunch program (National School Lunch Act).

The private business contribution requirement is met if the school district that established the qualified zone academy has written commitments from private entities to make "qualified contributions" having a present value as of the date of issue of the QZABs of not less than 10% of the proceeds of the QZAB issue. For this purpose, "qualified contributions" include (i) equipment for use in the qualified zone academy, (ii) technical assistant in developing curriculum or in training teachers in order to promote appropriate market driven technology in the classroom, (iii) services of employees as volunteer mentors, (iv) internships, field trips, or other educational opportunities outside the academy for students, or (v) any other property or service specified by the local education agency.

State Law Limitations. As previously discussed, a school district may not incur capital indebtedness without the prior approval of the requisite percentage of the voters voting on the matter at an election held for such purpose. This includes QZABs to which all constitutional and LFL restrictions apply.

The public sale of QZABs in New York State has been met with limited success but private sales/placements have been possible, provided that the size of the QZAB issue is $5,000,000 or less ($1,000,000 or less on or after June 1, 2012) or the bond structure includes some original issue discount. *See* Chapter 11.

Joint Projects and Cooperative Debt

There are various ways to accomplish this depending on the particular facts and circumstances. A library district should explore these kind of obligations with bond counsel if financing a joint project with another library or municipality is contemplated. Likewise for libraries with Joint Affiliated Entities. Article VIII Section 1 and Section 2-a of the Constitution, Title 1-A of the Local Finance Law and Article 5-G of the General Municipal Law are the main governing provisions.

Mortgage Notes of a Library District

We have noted that the issuance of general obligation debt secured by a security interest like a mortgage in a building or other asset of a political subdivision/local governmental unit such as an Affiliated Entity is not permitted under New York State Law. All of the above debt instruments authorized by the Local Finance Law are "general obligations."

However, both the Education Department and the Office of the State Comptroller have issued opinions that a library district can itself enter into a mortgage loan, which is not general obligation debt. The complete opinions in support of this view are presented here in the interest of providing the reader with the fullest available information on this view. Why such detail? Because it *is* surprising to anyone steeped in the constitutional, statutory and case law regarding the mortgaging of real property of political subdivisions in New York State and while a library district itself does not have the power to issue any debt types authorized in the Local Finance Law, like most political subdivisions it *does* have some power of taxation, a central attribute of independent local governmental units. It is betwixt and between, a hybrid corporate entity. Therefore, the authority to issue debt in the form of a mortgage note is somewhat unusual. Its statutory basis would seem to be the State Not-For-Profit Law, Articles 2 and 5, which are said to apply in relevant parts to a "domestic educational corporation" pursuant to Education Law Section 216-a (which may include a free association library), as well as Education Law Section

226(6), which specifically authorizes the mortgaging of property. It is *not* debt subject to the rules of the Local Finance Law, and a Library District (or a free association library) could issue one. The terms of a mortgage note would be determined by negotiation with the lender bank. The opinions are as follows:

Opinion 76-771 of the Office of the State Comptroller

Statement of Fact: A school district library currently utilizes a building owned by the school district. It is contemplated that expansion will be necessary in the future. The library's architect has advised that the most efficient way to accomplish this would be to build an addition on two adjacent lots which are privately owned.

While the library does not contemplate immediate construction, it would like to acquire such property now and use it for parking until needed for expansion. There is, however, some question as to whether the owner of the property will agree to sell, since there is a disagreement over price, and, in addition, one of the owners resides on the property and wishes to continue living there until he dies.

The library currently has an inappropriate surplus which has been accumulated over a number of years and which it would like to use for the purchase of the land. Furthermore, the library would like to acquire title to the land in its own name.

Inquiries: (1) May a school district library acquire title to property in its own name, without the approval of either the school board or the school district voters?

(2) Was it permissible for the library to accumulate the aforementioned surplus, and may it now be used to purchase the land?

(3) If the library cannot negotiate a mutually acceptable contract to acquire the lots in question, may it condemn the land and acquire title?

(4) If only the school district possesses the power of condemnation, what procedures should be utilized by the library to make its surplus funds available to the school district in order to pay the condemnation award?

(5) Assuming that the library is able to acquire title in its own name, is it correct to say that only the school district, and not the library, may issue obligations to fund the costs of construction of the addition on the land?

(6) May the library agree to accept title to one of such parcels, subject to a reserved life estate in favor of the present owner?

Statement of Law: (1) Education Law §260(1) provides that the board of trustees of a public library shall have all of the powers of trustees of other educational institutions chartered by the board of regents. Education Law §226 contains the powers of such trustees. Subdivision (6) thereof gives to such a board of trustees the power to "Buy, sell, mortgage, let and otherwise use and dispose of its property as they shall deem for the best interests of the institution ...." This would clearly authorize the board to acquire property in its own name without any approval of either the school district board of education or the school district voters (see 32 Op St. Compt. 30 (1976); 1972 Op St Compt #72-701 (unreported).

While the library may acquire the property in question without school district approval, it obviously cannot construct a building on such land which will be physically attached to a library building owned by the school district without the consent of the school board. Therefore, it would seem to be advisable for the library to obtain such consent now before land is acquired for such purpose.

(2) The Department has stated that a public library may accumulate surpluses from year to year and use such surpluses for lawful library purposes (1971 Ops St Compt ##71-804, 1010 unreported). Since the acquisition of land for the construction of a library building is a lawful library purpose, such surplus may be used for such purpose.

(3)While §226(6) gives to a public library the power to buy and sell real property, neither that section nor any other provision of law gives such libraries the power to condemn land for library purposes. In the absence of such statutory authority, the library obviously cannot exercise the power of condemnation.

While the library does not possess such power, the school district board of education is empowered to acquire property, by condemnation, "for school purposes, and for any other purpose for which such property may be acquired as provided [in the Education Law]" (Educ L §404(2).) Since Education Law §255(1) authorizes a school district which has established a school district library to acquire property for library purposes, §404 clearly authorizes the school district to condemn property for library purposes.

(4) If it is necessary to condemn the lots in question, the property will have to be obtained in the name of the school district. If this is the case, it will be necessary that the surplus funds of the library be made available to the school district to pay the condemnation award. This can be done, we believe, by the library board simply authorizing a transfer of the necessary amount from the library to the school district for that designated purpose.

(5) Although a public library is not authorized to issue obligations pursuant to the Local Finance Law, it is authorized by Education Law §226(6) to "mortgage" its real property. Therefore, if the library, as opposed to the school district, holds title to such land, it could mortgage such property in order to obtain funds to build a library facility thereon. Of course if title to the property in question rests with the school board, then it may not be mortgaged and the only way to borrow funds for construction on such land would be for the school district to issue obligations pursuant to the Local Finance Law.

While the library can mortgage its own property, it would probably be unable to do so in the present case since the building would be physically connected to buildings owned by the school district.

(6) This Department, in another opinion (28. Op. St Compt. 206 (1972), expressed the opinion that a county could acquire property subject to a reserved life estate. That opinion is equally applicable to a school district or a school district library. Therefore, either the library or the school district may acquire property in question subject to a reserved life estate. This does not mean, however, that it is necessarily advisable to do so. Where title to the land is acquired subject to a reserved life estate, it is possible that the land will not be available for use when needed (although, the school district, but not the library, could possibly condemn the reserved life estate and thus obtain immediate possession).

Conclusion: (1) A school district library may obtain title to real property in its own name, without the approval of the school board or the school district voters.

(2) A school district library may accumulate surpluses from year to year and use these to purchase land.

(3) Although a school district library cannot condemn real property for library purposes, the school district can.

(4) If it is necessary to condemn property for library purposes, a school district library may transfer accumulated surplus funds to the school district to pay for the condemnation award.

(5) While a school district library could not issue obligations pursuant to the Local Finance Law to finance the construction of a building on land owned by the library, it could, generally speaking, mortgage property to finance such construction.

(6) Either the school district library or the school district may acquire title to real property subject to a reserved life estate.

Opinion No. 82-127 of the Office of the State Comptroller.

Libraries—Capital Improvement (financing by means of mortgage loan)

Real Property—Mortgages (by school district public library to finance construction loan).

Capital Improvements—Financing of (by school district public library by means of mortgage loan)

Education Law, §s 226(6), 260(10): A school district public library may finance construction of an addition to the library, title to which is in the school district, by means of a mortgage loan if it acquires a leasehold interest in the building.

We have received a letter asking whether a school district public library may finance construction of an addition to the library building by means of a mortgage loan. We are informed that the building was financed through the issuance of obligations by the school district and that title to the building is in the school district.

Inasmuch as title to the building is in the name of the school district, we believe there is a threshold question of whether the school district must approve construction of the proposed addition. Section 260(10) of the Education Law provides, in pertinent part, that the board of trustees of the school district public library "shall have the power to determine the necessity for construction of library facilities." We have previously expressed the view that this provision obviates the need for school district approval of a proposed improvement to a school district-owned library building which is to be financed by the issuance of school district obligations (see Opns. St. Comp., 1980, No. 80-154).

Although it is our view that the need for obtaining prior consent of a school district on the issue of proposed improvements to the school district's library building has been eliminated by section 260(10), we note that section 408 of the Education Law requires that plans and specifications for construction of or improvements to school buildings must be approved by the Commissioner of Education. We have been informed by the Education Department that they generally require consent of school districts which own the library buildings prior to approving construction. They further inform us that approval of construction would not be denied where consent of the school district is *unreasonably* withheld.

With respect to the issue of financing construction of the addition by means of a mortgage loan, library trustees are vested with all the powers of trustees of other educational institutions (Education Law, §260(1)) which includes the power to mortgage library property as they deem to be in the best interest of the library (Education Law, §226(6)). Since title to the library building is in the school district, the library trustees clearly could not mortgage the title. However, it is well established that a leasehold interest in real property is a chattel real which may be mortgaged (see, generally, 38 NY Jur, Mortgages and Deeds of Trust, §40).

School district public libraries which do not hold title to the library building in their own name would generally not enter into a formal lease agreement for the use of the building with the school district. This is because for purposes of use of the school district's property the library is a department or agency of the district and no formal lease agreement is necessary. Nonetheless, while a formal lease would not be necessary, we are aware of no legal impediment to a school district and its library entering into such an agreement with respect to the building being used by the library. The lease could be entered into without consideration (see *Comereski v. City of Elmira*, 308 NY 248; *U.F.S.D. No. 3 v. Town of Rye*, 280 NY 469; Opns St Comp, 1981, No. 81-81).

Once the library trustees have acquired a leasehold interest in the building, they may mortgage that interest pursuant to the authority granted by section 226(6) of the Education Law. In light of the fact that the school district has title to the building, the mortgagee may require the district to subordinate its interest in the building to the mortgage. Since there is no prohibition against a gift of property from one public corporation to another (see the *Comereski* and *U.F.S.D. No. 3, supra*), it is our opinion that the school district could enter into a subordination agreement.

May 10, 1982

Mr. Robert H. Finkelstein, Board of Trustees

Finkelstein Memorial Public Library

Opinion of the Education Department

May 10, 1935 Case No. 3100

50 Op. St. Dept. 507 (1935)

(relevant portion only; Section 68 is predecessor to current Section 226)

The library board has broader powers. It cannot be doubted that such a corporation has the general power to borrow not limited to the possible receipt of public money or of uncollected taxes. (*Matter of Hyde v. Equitable Life Assur. Soc*., [1908] 61 Misc. 518; *Partridge v. Badger*, [1857] 25 Barb. 146; *Kent v. Quicksilver Mining Co.*,[1879] 78 N.Y. 159; *Furniss v. Gilchrist*, 1 Sandf. 53; *Curtiss v. Leavitt*, 15 N.Y. 9, 219; *Mead v. Keeler*, 24 Barb. 20.) While it may be that such library board would need some collateral upon which to borrow, nevertheless the necessity for the same must be determined by the lending agency.

Furthermore, attention is called to the provisions of section 68 of the Education Law, which states, generally, the powers of corporations created by the Board of Regents. Under subdivision 6 of this section the library board has the power to sell, buy, mortgage, let and *otherwise use* and dispose of its property. While this subdivision does not specifically contain the expression "borrow," certainly such term is included in the other general terms used in the section.

Thus, according to Opinion of the Education Department, 50 St. Dept. 507 (1935), the language of Section 226(6) (actually its exact predecessor Section 68 of the Education Law) is meant to include the authority to borrow in connection with a mortgage of property. And as noted above, the office of the State Comptroller in 1982 in Opinion 82-127 held that a school district public library could finance construction by means of a mortgage loan. *See also*, Opin. St. Compt. 76-199 which holds payments on a purchase money mortgage are a "lawful purpose" of a school district public library. Note: Such opinions are advisory.

Let us be quite clear then on what these opinions provide: a library district (or a free association library) has authority to borrow money in the form of a mortgage note which is a form of debt obligation that is *not* subject to the amortization, sale, pledge, and related rules of the Local Finance Law discussed in Chapters 9, 10 and 11 of this primer, which *are* applicable to debt issued by an Affiliated Entity, when issued on behalf of a Library District or municipal library. The structure of a loan evidenced by a mortgage note and the procedures for its issuance are between a Library District (or free association library) and its lender. Such debt cannot be "general obligation" debt, which depends on the "faith and credit" pledge of the "unlimited taxing power" of a local government. Why not? Because, it is not debt issued pursuant to the Local Finance Law. A Library District (or a free association library) cannot itself issue debt authorized by the Local Finance Law. A Library District *can* cause the levy of a tax, **but its power to tax is not unlimited, with regard to the payment of debt service or otherwise**. That is a critical difference. However, a Library District does have a reliable stream of revenues that it could pledge to a bank, even though it cannot pledge its "faith and credit." A pledge of a specific stream of tax revenue is not the same as the pledge of an unlimited power to tax. Again, a critical difference. And a free association library may have a reliable stream of revenue that it could pledge to a bank, from the approved municipal support in its budget, for example.

CHAPTER TEN

Amortization Structures

In New York State, there are rules regarding when principal must first be paid, when principal may last be paid, and how often and how much may and must be paid between the two dates, for all general obligation debt. (This does not apply to mortgage notes, the terms of which are governed solely by the agreement of the parties.)

The New York State Constitution has long provided that no installment for the payment of principal of outstanding indebtedness of any municipal issuer may exceed any prior installment by more than fifty percent. This provision has generally meant that the debt service requirements for any particular general obligation municipal debt in New York declined with time, as the decline in annual interest due overtook any limited permitted annual increase in principal repayment. The point was to ensure that debt was not back-loaded to future generations of property taxpayers.

In 1993, that provision of the Constitution was amended, effective January 1, 1994. All municipalities, school districts and district corporations in New York State may now, consistent with the Constitution, alternatively contract to repay indebtedness in substantially level or declining annual debt service payments.

Paydown of Principal Options. There are a few basic legal rules in this regard that must be considered:

a. ***The 2-Year Rule:*** An Affiliated Entity (and thus a Library District) must begin to pay down principal within two (2) years of the original date of issuance, but may voluntarily pay down its first principal earlier. (If a local government delays in the case of five year items like vehicles, it does substantially increase what the last four payments will look like.)
b. ***Annual Principal:*** Thereafter, principal *must* be paid down annually. (That means not so little as one day beyond the anniversary date.)
c. ***Method of Amortization of Annual Principal:*** As noted above, there are two methods for determining the overall structure of debt service over the payoff period: (1) what is known as "50% rule debt" in which principal is structured according to the Constitutionally-based rule that no principal payment over time may exceed any

prior smaller principal payment by more than 50%. This rule was designed to prevent excessive back loading of principal payoffs onto later generations of taxpayers, or (2) substantially level annual debt service in which principal and interest payments are substantially equal in each year (not usually perfectly equal) similar to home mortgage payments except that BANs usually pay interest and principal annually and bonds usually pay interest semiannually and principal annually.

d. ***Length of Amortization:*** The period of probable usefulness of a capital project establishes the outside date by which all debt for the project must be paid off, set by the date of the first borrowing therefor.

The "Two-Year Rule" for Bond Anticipation Notes

A principal payment must be made with respect to bond anticipation notes within two years of the date of issuance of the first bond anticipation note. That principal payment should be sized with the "fifty percent" rule in mind, or after determining to implement level annual debt service.

The "Two-Year Rule" for Bond Issues

If an Affiliated Entity does not issue bond anticipation notes on behalf of the Library District, but instead goes directly to a bond issue, the first principal payment of a bond issue must fall within two years of the date of the bonds.

Put another way, the rule is that the first principal payment with respect to any financing must be made within two years of the date of the first bond anticipation note or within two years of the date of the bonds.

The 50% Rule

The general rule is that no principal payment during the course of bond anticipation note financing or serial bond financing may exceed by more than fifty (50%) percent, the smallest previous principal payment.

Thus, when a Library District plans on making a principal payment during the course of bond anticipation note financing, the Library District wants to make sure that that principal payment is sufficient enough to allow the Library District to amortize the future bond issue of its Affiliated Entity over the remaining years allowed without any of the future principal payments exceeding by more than fifty percent that next principal payment that the Library District is planning to make.

In the case where the period of probable usefulness is in excess of five years, and the bond resolution does not restrict the maximum maturity thereof to five years, and it is planned to finance that purpose over a period in excess of five years (i.e., common Library District building projects), the general rule is that serial bonds must be sold, issued and delivered within five years of the date of issuance of the first bond anticipation note, with the first maturity of such serial bonds falling on or before the date that marks the end of the five-year period computed from the date of issuance of the first bond anticipation note.

A principal payment from a source other than the proceeds of bonds or bond anticipation notes must be made within two years of the date of issuance of the first bond anticipation note and the amount of that principal payment and the amount of each subsequent principal payment should be sufficient so as to allow the Affiliated Entity to pay off the balance of the financing over the remaining period of years allowed to it without violating the so-called “50% rule.”

The 50% rule, simply stated, says that no principal payment of indebtedness, whether made in the course of bond anticipation note financing or in a serial bond maturity schedule, may exceed by more than 50% the smallest of any of the previous principal payments.

A simple illustration: a Library District has a $100,000 purpose that can be financed, according to the term specified in the bond resolution, over ten (10) years. It makes a first principal payment of $8,000. Because the 50% rule permits the Library District now to go as high as $12,000 on any subsequent payment, it is obvious that, whether or not a principal payment is made at the end of the first year of bond anticipation note financing, the Library District will be able to pay off the indebtedness over the period remaining to it eight (8) years in the first case, nine (9) years in the second) without violating the 50% rule.

Compare another Library District, with the same $100,000 purpose, which makes a first principal payment of $6,000 instead of $8,000. Under the 50% rule, the $6,000 payment limits the Library District to a maximum payment of $9,000 in any subsequent year. Assuming that the $6,000 payment was made at the end of the second year (no payment having been made at the end of the first year), the Library District now has eight years of payment left. Taking these 8 years and multiplying 8 x $9,000, you arrive at $72,000; and one can see, this $72,000 plus the original $6,000 payment ($78,000) makes it impossible for the Library District to pay off the financing by the end of the ten-year period without violating the 50% rule.

The 50% Rule and Seeming Violations

Under certain circumstances bond counsel can approve the legality of bond anticipation notes which, on their face, seem to violate the so-called fifty percent rule described above.

Assume that a Library District had issued on its behalf a bond anticipation note in the principal amount of $330,000 for a building reconstruction project in “Fiscal Year 1.” This was the first note issued for the project. The bond resolution limited the maximum maturity of the serial bonds to five years. (It would never happen, but imagine it for purposes of a simplified illustration.)

In the following fiscal year (“Fiscal Year 2”), against the outstanding $330,000 bond anticipation note then maturing, the Library District made a principal payment in the amount of 66,000, such amount constituting the first installment of such indebtedness, and issued a renewal note in the principal amount of $264,000.

Similarly, in the next succeeding fiscal year (“Fiscal Year 3”), the Library District made a principal payment in the amount of $66,000 and issued a renewal note in the principal amount of $198,000.

The Library District then advises bond counsel for the Affiliated Entity that they would now like to pay off entirely the outstanding $198,000 bond anticipation note at the time of its maturity and asks whether this would be legal in view of the so-called "fifty percent rule."

The answer to that question is unequivocally in the affirmative: the Library District legally may make such a payment. The rationale lies in the distinction between "voluntary" payments and "involuntary" or "mandated" payments.

Pursuant to Section 53.00 of the LFL, an Affiliated Entity may issue obligations on behalf of the Library District which are redeemable prior to maturity. Thus, for example, a School District could issue a $2,000,000 bond issue payable $100,000 per year over a period of twenty (20) years with the bonds callable at the end of the tenth year. Assume that that serial bond issue was issued by a current administration in office at a School District in Fiscal Year 1 with a 10-year call feature. The provisions for early redemption do not mandate upon the administration which is in office in year ten (10) the decision to call in the bonds at that time; the decision to call in the bonds in Fiscal Year ten (10) by the administration in office in that year is an entirely voluntary decision directed by the Library Board of Trustees and not mandated by law or any other circumstances.

If one accepts the constitutionality of the provisions of the LFL which permit the issuance of callable bonds and which allows an administration ten years after issuance to voluntarily pay off the balance of the bonds, thus seeming to violate the so-called "fifty percent rule," then one must accept the constitutionality and legality of an issuer voluntarily deciding to pay off a bond anticipation note in the circumstances which are described above.

It is important to note: voluntary payments can only be said to be constitutional and legal where the previous payments have been of such sufficient magnitude so as not to have mandated the issuer into having to make a payment which violates the fifty percent rule in order to amortize the issue over the remaining allowable maturity.

Thus, for example, in the instant situation, if the School District had paid $66,000 in Fiscal Year 2 and then in Fiscal Year 3 lowered that payment down to $30,000, one can see that under the fifty percent rule no subsequent payment could exceed $45,000 and to enable the School District to pay off the financing within the allowable 5-year maturity period (computed from the date of issuance of the first bond anticipation note), the School District would be forced (mandated) to make a principal payment within such 5-year period of such a magnitude so as to result in a violation of the fifty percent rule.

Accordingly, it follows that whether a payment may be regarded as being "voluntarily" made or "involuntarily" made depends upon the size of the principal payments that have been made during the course of the financing up to the date that the School District is considering the payment which, on the face of it, would seem to violate the fifty percent rule.

Now consider a different set of circumstances when a principal payment has been made after the first year of bond anticipation note financing which seemingly violates the so-called 50% rule set forth in paragraph d of Section 21.00 of the Local Finance Law.

Paragraph b of Section 23.00 of the Local Finance Law provides that bond anticipation notes shall mature within one year from the date of their issue and may be renewed from time to time, but each renewal shall be for a period not exceeding one year and in no event shall such notes or the renewals thereof extend more than two years beyond such original date of issue unless a portion of such notes or the renewals thereof shall be redeemed from a source other than the proceeds of bonds within two years from such original date of issue.

In plain English, as discussed earlier, this means that you must make a principal payment within two years of the date of issuance of the first bond anticipation note.

By omission, then, the statute permits a Library District to make no payment at the end of the first year and roll over the bond anticipation note in full.

Let us take a $100,000 financing with a 10-year maturity as an example. The municipality issues $100,000 bond anticipation note in year one. At the end of year one, the district makes a $10,000 principal payment and issues a $90,000 renewal note. At the end of year two (the year in which a principal payment is mandated by the statute) the district makes a $5,000 principal payment.

Bingo!—you have an automatic violation of the 50% rule, because the 50% rule says that no principal payment may exceed by more than 50% the smallest previous principal payment mandated by law. By making the principal payment in the amount of $5,000, no subsequent payment may legally exceed $7,500, and you can see that over the next eight years, it is impossible to amortize the remaining $85,000 without violating the 50% rule.

Take a different scenario, however: At the end of the first year, the district makes a $5,000 principal payment. The uninitiated would conclude, using the reasoning above, that there is an automatic violation of the 50% rule. This is not the case. After all, the Local Finance Law provides that no principal payment need be made at the end of year one. If that is the case, then why should a library district be punished for making a "voluntary" payment at the end of year one. Thus, for the purpose of the 50% rule, one can disregard the first payment in this case, since it was voluntary payment not mandated by law.

Level Debt Service

Since January 1, 1994, the LFL provides for the issuance of bonds with substantially level or declining annual debt service, as an alternative to compliance with the "fifty percent" rule described above. This provision also allows use of the weighted average period of probable usefulness of various capital projects in the case of a consolidated bond issue in which a single bond issue is sold for multiple projects. If bond anticipation notes are issued for a project or projects for which it is anticipated that serial bonds will be issued with substantially level or declining annual debt service, such notes must be redeemed in part in each year in an amount at least equal that which an annual installment of hypothetical substantially level or declining serial bonds would be if issued at a five percent rate of interest. Compliance with the "fifty percent" rule during bond anticipation note financing prior to the issuance of serial bonds should generally comply with this requirement but should always be verified.

Bond Counsel should always be consulted as to exactly how "substantially level or declining annual debt service" should be implemented. If it is not done properly, the debt is not validly issued.

Note the relationship of the PPU calculation discussed earlier to a level debt service amortization: in the level debt service context, each object or purpose with its own PPU, in effect, "pulls its own weight" to be part of a resultant average aggregate maximum PPU. In this context, while a project with a 5-year useful life may be paid for, in effect, over ten (10) years, so too is a building with a 25-year useful life.

Relationship of Bond Anticipation Notes to Bonds: The "Five-Year" Rule

Generally, serial bonds must be sold, issued and delivered within five years of the date of issuance of the first bond anticipation note. An Affiliated Entity must arrange to sell the bonds sufficiently in advance of the five-year anniversary date so that the first maturity of the serial bonds will fall within five years of the date of the first bond anticipation note. This is a trap for the unwary.

Series Financings

It is possible to divide a financing into series of notes and series of bonds.

Assume that a school district has authorized an issue of $10,000,000 for a Library District and in the first year they only wish to issue $5,000,000 and follow that up in the second year by another $5,000,000 note issue. In the third year, they plan to consolidate the two borrowings into one serial bond issue. This will save interest expense.

In each case, each of the series (let us call them Series A and Series B) would stand on their own as separate issues; each series would have its own two-year rule; each series would have its own five-year rule; each series would have its own 50% rule; however, it is important to remember that the maximum maturity of the Series B financing would have to be pegged from the date of issuance of the first bond anticipation note (or serial bonds, if no such notes were ever issued) issued for the Series A financing. Within the single consolidating bond issue in year three, these rules must be observed.

CHAPTER ELEVEN

Public or Private Sale of Debt Instrument

The sale of BANs and serial bonds can involve private local placement or public competitive sale, but if over five million dollars ($5,000,000; $1,000,000 on or after June 1, 2012 when a temporary exception authorized by Chapter 386 of the Laws of 2010 expires), competitive sale of bonds (not notes) is legally required at this time with few exceptions. Unlike bonds, BANs may be sold at public competitive sale or privately placed with local banks or regional investment banking houses, regardless of the size of the issue. Note: Serial bonds can only be privately placed if they presently do not exceed five million dollars in principal amount ($1,000,000 on and after June 1, 2012) with few exceptions. One of the roles of a financial advisor is to assist in the determination of how to sell the debt, between the legally available options. (This chapter is pretty dry and boring but it is useful to read it just once.) In case you don't, here is an executive summary:

- An Affiliated Entity can sell bond anticipation notes in any amount either by competitive public sale with the help of a financial advisor or locally placed with a bank, with which you or they have a depository relationship. Get three bids, if possible.
- An Affiliated Entity can sell up to five million dollars of serial bonds annually (up to $1,000,000 only on or after June 1, 2012) locally with a bank, often a bank with which you or they have a depository relationship. Get three bids, if possible.
- Any bond issue of over $5,000,000 ($1,000,000 on and after June 1, 2012) must be sold publicly competitively following detailed statutory law and State Comptroller's regulations. Most will need a financial advisor to help you access this market.
- An Affiliated Entity can sell debt for certain types of capital improvements and equipment to the Dormitory Authority of the State of New York.
- A free association library is not subject to these rules.
- These rules do not apply to mortgage notes.

Note Sales

Notes (BANs, BARNs, TANs, RANs, capital notes and budget notes) may be sold at public competitive sale or privately placed regardless of the size of the issue. If sold publicly, the notice of sale must conform to the requirements of Section 60.00 of the LFL and the State Comptroller's rules found in Part 26 of Chapter II of the Title 2 of the N.Y. Comp. Codes Rules and Regulations (hereinafter, "N.Y.C.R.R."). If privately placed, it is recommended that bids be solicited from at least three institutions, e.g., local banks, assuming three banks still do business in the area. This is not a legal requirement.

The basic note sale rules are as follows:

a. Notes may be sold at either public or private sale, but they cannot generally be sold on option or on a deferred payment plan.
b. Notes may be sold without limitation as to rate of interest, and generally for a sum not less than the par value of, and the accrued interest on, such obligations, and bond anticipation notes may be sold to the state of New York municipal bond bank agency, at such rate or rates of interest as may be agreed upon by and between the issuer and such agency.
c. Capital notes for one or more specific objects or purposes or classes of objects or purposes, or a combination thereof, may be sold as a single capital note issue. Bond anticipation notes for one or more specific objects or purposes or classes of objects or purposes, or a combination thereof, may be sold as a single bond anticipation note issue. This is known as a consolidated issue.
d. If notes are sold at public sale the board of education may specify the procedure therefore or they may adopt as much of the procedure prescribed for the sale of bonds in sections 57.00 to 59.00 inclusive, of the LFL, as they may desire. In all such sales, however, the provisions of paragraph e below must be complied with. Nothing in the rules prevents the sale of notes at public auction.
e. The State Comptroller has adopted regulations, prescribing a procedure for the circularization of notices for the public sale of notes and which also prescribes such data and information that his office deems advisable to be contained in such notices. It is a part of the job of bond counsel to ensure compliance with those regulations.

Smaller note issues are often privately placed after an informal solicitation process with local banks, particularly depository banks of the issuer. What constitutes small is basically a matter of the appetite of your local banks for local governmental debt. When notes are sold by competitive sale or are to be sold privately in the larger financial markets, the services of a financial advisory firm are usually engaged.

Public Bond Sales

Bonds of over five million dollars ($5,000,000; $1,000,000 on or after June 1, 2012. Chapter 386 of the Laws of 2010 has authorized private sale of bonds up to $5,000,000 until June 1, 2012.) in principal amount may be sold only at public sale and in accordance with the procedures set forth in Sections 57.00, 58.00 and 59.00 of the LFL with few exceptions as noted below. A debt statement must be filed with the Office of the State Comptroller before the public sale of most bonds (but not notes) in accordance with the requirements and procedures specified in Title 10 of the LFL.

The basic bond sale rules are as follows:

a. Bonds issues of over five million dollars ($5,000,000; $1,000,000 on and after June 1, 2012) shall be sold only at public sale and in accordance with the procedure set forth in the LFL, except as described below.
b. Bonds may be sold at private sale in any authorized amount to the United States government or any agency or instrumentality thereof (such as the Department of Agriculture, Rural Development Division), the State of New York Municipal Bond Bank Agency, to any sinking fund or pension fund of the municipality, school district or district corporation selling such bonds, or, in the case of bonds or other obligations of a municipality issued for the construction of any sewage treatment works, sewage collecting system, storm water collecting system, water management facility, air pollution control facility or solid waste disposal facility, also to the New York State Environmental Facilities Corporation ("EFC") and school districts and certain other entities may sell such debt to the Dormitory Authority of the State of New York.
c. Bonds may also be sold at private sale as provided in Section 63.00 of the LFL if five million dollars ($5,000,000) and under ($1,000,000 on and after June 1, 2012), hereinafter described.
d. No bonds shall be sold on option or on a deferred payment plan, except that options to purchase, effective for a period not exceeding one year, may be given in certain very limited cases, including to EFC with respect to bonds or other obligations issued for the construction of any sewage treatment work, sewage collecting system, storm water collecting system, water management facility, air pollution control facility or solid waste disposal facility. A loan commitment may also be entered into by and between a county and the State of New York Municipal Bond Bank Agency and by and between such a municipality and EFC, such commitment to be fulfilled by the purchase of the bonds or other obligations by such state agency or such state corporation.
e. Bonds shall be sold without limitation as to rate of interest and for a sum not less than the par value of, and the accrued interest on, such obligations except as authorized by the LFL, and may also be sold at private sale to the State of New York Municipal Bond Bank Agency and to EFC and to the Dormitory Authority of the State of New York in certain cases. *See* "The Role of the Dormitory Authority" in Chapter 21 for a discussion of "Dorm" financing programs for school districts and for libraries. When sold at public sale, the rate of interest shall be determined in the manner provided in Section 59.00 of the LFL. A maximum rate of interest at which such bonds shall be sold may be fixed.
f. Bonds for one or more specific objects or purposes or classes of objects or purposes,

or a combination thereof, may be sold as a single bond issue. This is known as a "consolidated bond issue."

g. The state comptroller has adopted rules with which bond counsel ensures compliance.
   1. Designating a financial newspaper or newspaper published and circulated in the city of New York in which notices for the sale of bonds may be published;
   2. Prescribing the procedure for the circularization of notes for the sale of bonds;
   3. Prescribing certain other requirements as necessary relating to the publication or circularization of notices for the sale of bonds;
   4. Prescribing certain data and information with which both bond counsel and the financial advisor are familiar; and
   5. Prescribing the requirements for the alternative and permissive publication or circularization of notices particular to the sale of bonds of an issue not exceeding five million dollars ($5,000,000; $1,000,000 on and after June 1, 2012).

   It is part of the duties of bond counsel and the financial advisor to the school district to ensure compliance, and to assist with the filing of a debt statement with the office of the State Comptroller prior to the bond sale.

h. Notwithstanding the limitations set forth above, a municipality or village may provide for the public sale of its bonds at a price of less than the face value of such bonds at maturity i.e. at an original issue discount such that the issuer does not receive full face amount of principal; provided that no issue of bonds shall be sold at a price such that the difference between the sale price of such bonds, not including accrued interest, and the face value of such bonds at maturity, shall exceed five percent of the face value of such issue of bonds at maturity unless the municipality, village or district corporation issuing such bonds has determined to issue them pursuant to a substantially level or declining annual debt service schedule or unless interest is contributed at least annually to a sinking fund in accordance with section two of article VIII of the constitution and the procedures of Section 22.10 of the LFL. The cost of such original issue discount, together with other costs of the issuance of obligations, is deemed a part of the cost of the object or purpose for which such obligations are issued.

Public Bond Sale Notice

The rules for the notice of sale of bonds are as follows:

a. There must be published, at least once, not less than five nor more than thirty days before the date fixed for public sale of bonds, a notice of such public sale or a summary thereof in accordance with one of the following methods:
   1. the notice of sale shall be published in any financial newspaper published and circulated in the city of New York which the State Comptroller has designated for such publication as *The Daily Bond Buyer*;

2. the notice of sale shall be circularized in such manner as the state comptroller has prescribed and shall be published in any newspaper or newspapers which the board of education may designate for such purpose; or
3. (i) a summary of the notice of sale shall be published in both the financial newspaper published and circulated in the city of New York which the state comptroller has designated as *The Daily Bond Buyer*, and (ii) any newspaper or newspapers which the board of education may designate for such purpose. A summary of the notice of sale at a minimum must contain the name of the issuer, the amount, date, and maturities of the bonds, the frequency of interest payments, the place where bids will be received, including the designation of the receiving device if the board of education has authorized the receipt of bids in an electronic format, the time and date for the opening of the bids, including circumstances under which such time and date may be changed in accordance with law, the method of award and a procedure for promptly obtaining the complete notice of sale and any preliminary official statement prepared in connection with the sale, and certain other information that the State Comptroller requires.

b. Such notice shall call for sealed bids for the purchase of such bonds, and shall state:
1. The place where bids will be received and considered, and the designation of the receiving device for electronic bids if the board of education has authorized same.
2. (a) The time and date for the opening of bids, which shall be only on weekdays, Saturdays and holidays excluded, between the hours of 10:00 A.M. and 4:00 P.M.
(b) In lieu of the statement of the time and date for the opening of bids, a statement (i) that the time and date for the opening of bids will be provided on not less than twenty-four hours prior notice by means of a supplemental notice of sale and indicating the manner in which such supplemental notice will be provided, or (ii) setting a time and date for the opening of bids, stating that notice of a change in time or date for the opening of bids may be provided not less than twenty-four hours prior to the time originally scheduled for the opening of bids by means of a supplemental notice of sale and indicating the manner in which such supplemental notice will be provided. Where notice is given that the time or date of a sale will be changed without specifying the new time or date, notice of the new time or date of sale must be provided by means of a second supplemental notice of sale at least twenty-four hours prior to the new time for the opening of bids.
(c) A supplemental notice of sale must refer to and be deemed a part of the notice of sale and must not establish or change the terms of the sale other than the time or date for the opening of bids, the amount of principal scheduled to be repaid in each year, the right or redemption prior to maturity, and the face value at maturity of the issue or any installment thereof. The time set for the opening of

bids in the supplemental notice of sale must not be less than five nor more than thirty days after publication of the notice of sale.

(d) The supplemental notice of sale must be provided by transmittal over a definitive trade wire service of the municipal bond industry which, in general, makes available information regarding activity and sales of municipal bonds and is generally available to participants in the municipal bond industry, or by publication in the financial newspaper published and circulated in the city of New York which the state comptroller, designates for such publication in regulations. In addition, public notice of the time and date set for the opening of bids in the supplemental notice of sale shall be given to the news media and must be posted in one or more designated public locations within the issuing school district at least twenty-four hours prior to the time and date set for the opening of bids; provided, however, that such public notice is not to be construed to require publication as a legal notice.

3. The maximum rate of interest, if any, that may be bid.

c. Such notice must also include:

1. A statement that the rate or rates of interest to be bid shall be a multiple of one-hundredth of one per centum per annum or a multiple of one-eighth of one per centum per annum, as the offices in charge of the sale may determine and may require or permit in such notice.

2. A statement of the conditions of sale and the methods of bidding which must include the following:

a. A statement that one or more than one rate of interest may be bid; provided, however, that only one rate of interest may be bid for bonds of the same maturity. Where more than one rate of interest may be bid, such notice shall specify the maximum number of rates which may be bid. Where the net interest cost method of calculating interest cost is used, or where the notice so provides, the interest rate for each maturity shall not be less than the interest rate for any prior maturity. Such notice shall also state that such rate or any of such rates may not be higher than the maximum rate prescribed in such notice, if a maximum rate has been prescribed. Notwithstanding the above, in inviting proposals for the sale of bonds in an amount of twenty million dollars or more, a school district or municipality may advertise in such notice to sell, in series, at a single bid price per bond.

b. Where two or more issues are offered in the same notice of sale, a statement specifying whether each of the issues so offered shall be sold separately as a single bond issue, whether some of the issues shall be combined and sold separately as one or more single bond issues, or whether the aggregate amount of bonds of all of the issues shall be combined and sold as a single bond issue.

c. Where the governing board of the issuer has determined to provide for substantially level or declining annual debt service, a statement specifying the dates of maturity for such bonds and the dates for payment of interest on such bonds, and setting forth the annual principal installments expected to provide for, together with the interest thereon, substantially level or declining annual debt service on such bonds. Such notice shall state that the issuer may, after selecting the low bidder, adjust such installments to the extent necessary to meet the requirement of substantially level or declining annual debt service.

3. A requirement that as a condition precedent to the consideration of his or her bid, each bidder shall deposit with the official of the issuer in charge of the sale, a certified or cashier's check drawn upon an incorporated bank or trust company to the order of the issuer or such official, for not less than one per centum of the amount of bonds to be bid for. Such notice may also provide that, in lieu of a certified or cashier's check, bidders may furnish as security an eligible surety bond or an eligible letter of credit, approved by such official as to form, sufficiency, and manner of execution. "Eligible surety bond" means a bond executed by a insurance company authorized to do business in this state, the claims-paying ability of which is rated in the highest rating category by at least two nationally recognized statistical rating organizations; and "eligible letter of credit" means an irrevocable letter of credit issued in favor of the municipality or school district, for a term not to exceed ninety days by a bank, as that term is defined in section two of the banking law, whose commercial paper and other unsecured short-term debt obligations (or, in the case of a bank which is the principal subsidiary of a holding company, whose holding company's commercial paper and other unsecured short-term debt obligations) are rated in one of the three highest rating categories (based on the credit of such bank or holding company) by at least one nationally recognized statistical rating organization or by a bank that is in compliance with applicable federal minimum risk-based capital requirements.
4. A statement that there is reserved to the issuer the right to reject all bids, and that any bid not complying with the terms of the notice will be rejected.
5. A statement that the issuer has reserved to itself the power to call in and redeem a portion of such bonds prior to their date of maturity, if it has reserved to itself such power (a so-called "early redemption" provision). Such statement shall identify the portion of the bonds which may be so redeemed and shall describe the terms and conditions under which such bonds may be redeemed.
6. A statement indicating which of the methods set forth in paragraph a of Section 59.00 of the LFL (described below) will be used in awarding such bonds.
7. Certain further data and information required by the State Comptroller.

d. It may be a condition of the sale of bonds that every bidder may be required to accept a portion of the whole amount of the bonds for which he has bid, at the same rate for such portion as may be specified in his bid for the full amount. If such condition is imposed, the notice of sale shall so state and such notice also shall state that, in addition, any bidder may offer to purchase all or none of such bonds on different terms.

e. The notice of sale may provide that the bidder to whom the bonds are to be awarded, at his option, may refuse to accept the bonds if prior to the delivery of the bonds any income tax law of the United States of America shall provide that the interest on such bonds is taxable, or shall be taxable at a future date, for federal income tax purposes, assuming the bonds were sold as federally tax-exempt.
f. Until June 1, 2013 sealed bids can include bids submitted in electronic format but not as a sole method and this method must be in compliance with certain statutory rules.

The bid opening and award process is also governed by statute, being Section 59.00 of the LFL, with the following rules:

Bid Opening and Award Rules

a. All bids must be opened publicly at the time and place stated in the notice of sale, and not before, and shall be publicly announced. Prior to the time fixed for such public opening of bids, a sealed bid may be amended by a bidder by delivery to the official to whom the sealed bid was delivered of a sealed amendment to such bid. No bid can be amended by a telegraphic or telephonic communication (except electronic bids may be amended by same method). The bonds are to be awarded to the bidder offering the lowest interest cost to the issuer, as computed in accordance with the net interest cost method or the actuarial or true interest cost method as duly noticed in the notice of sale.
b. If it is a condition of the sale of bonds that every bidder may be required to accept a portion of the whole amount of such bonds for which he has bid, at the same rate for such portion as may be specified in his bid for the full amount then any bidder may, in addition, offer to purchase all or none of such bonds on different terms.
c. When the bidder to whom the bonds are to be awarded has been ascertained, the municipality, school district or district corporation must promptly return all security to the persons furnishing the same, except the security furnished by such bidder. Such bidder must be promptly notified of the award to him, and if he refuses or neglects to pay either the agreed price for the bonds less the amount of any certified or cashier's check furnished as security, or the agreed price in full for the bonds if an eligible surety bond or eligible letter of credit was furnished as security, the security furnished by him, in whatever form, shall be forfeited to and retained by or claimed against or drawn upon by, the issuer as liquidated damages for such neglect or refusal. However, if the notice of sale shall contain the notice and if prior to the delivery of the bonds any income tax law of the United States of America shall be revised to provide that the interest on such

> bonds is federally taxable, or shall be so taxable at a future date, for federal income tax purposes, and the debt had been sold as federally tax-exempt then, at the request of such bidder the security accompanying his bid must be returned to him and he is to be relieved of his contractual obligations arising from the acceptance of his bid.

Bond Interest Rates

While the LFL provides that bonds must be sold without limitation as to rate of interest and for a sum not less than the par value of, and the accrued interest on, such obligations except as authorized by the LFL, this does not preclude establishing certain bidding parameters in a public competitive bond sale. Here is an example:

> Each bid must be for all of said bonds and may state a single rate of interest or different rates of interest for different maturities, provided, however, that (i) only one rate of interest may be bid for bonds of the same maturity, (ii) the maximum difference between the highest and lowest interest rate bid may not exceed one and one-half per centum per annum, (iii) variations in rates of interest so bid shall be in ascending progression in order of maturity so that the rate of interest on any single maturity of said bonds shall not be less than the rate of interest applicable prior to maturity, and (iv) all rates of interest bid must be stated in a multiple of one-eighth or one-hundredth of one per centum per annum. Unless all bids are rejected the award will be made to the bidder complying with the terms of sale and offering to purchase said bonds at such rate or rates of interest as will produce the lowest net interest cost computed in accordance with the net interest cost method of calculation, that being the rate or rates of interest which will produce the least interest cost over the life of the bonds, after accounting for the premium offered, if any.

The purpose of such limitations is to prevent surprises like a 25% interest rate in one maturity counter-balanced by low rates later.

Bonds may also be sold by school districts at private sale to the State of New York Municipal Bond Bank Agency or to the EFC, or to the Dormitory Authority of the State of New York, each in accordance with particular programs such rate or rates of interest as may be agreed upon by and between the issuer and any such agency or corporation, as the case may be. *See* "The Role of the Dormitory Authority" in Chapter 21 for a discussion of "Dorm" financing programs for school districts and libraries.

When sold at public sale, the aggregate rate of interest shall be determined in the manner provided in Section 59.00 of the LFL computed as net interest cost or true interest cost as provided in the notice of sale. A maximum rate of interest at which such bonds shall be sold may be fixed by the issuer.

Sale of Bond Issues of Five Million Dollars or Less

When sold at public sale, bonds of an issue not exceeding five million dollars (one million dollars on or after June 1, 2012), whether of a single issue or sold as a single issue pursuant to paragraph c of section 57.00 of the LFL, having a maximum maturity of not more than five years measured from the date of the bonds, need not be sold in accordance with the requirements of Section 58.00 of the LFL , described above, for publication of the notice of sale but may be sold upon such publication or circularization of the notice as shall be prescribed by the State Comptroller in regulations.

Bonds of an issue not exceeding five million dollars (one million dollars on and after June 1, 2012), whether of a single issue or sold as a single issue pursuant to paragraph c of section 57.00 of the LFL, may also be sold at private sale without limitation as to rate of interest, provided, however, that the total amount of bonds which may be sold at private sale in any fiscal year of the issuer cannot exceed five million dollars (one million dollars on and after June 1, 2012). The 5-year limit does not apply to private sales.

Private Sales of Bonds Including Sales to the Dormitory Authority

As described above, bonds of an issue not exceeding five million dollars (one million dollars on and after June 1, 2012) may be sold at private (negotiated) sale as provided in Section 63.00 of the LFL, without limitation as to rate of interest, provided, however, that the total amount of bonds which may be sold at private sale in any fiscal year of a school district may not exceed five million dollars (one million dollars on and after June 1, 2012). This permits any school district to privately place such bonds, or informally solicit bids locally without any of the formal notice requirements described above for competitive sales of bonds.

Bonds may also be sold at private negotiated sale with original issue discount as described earlier or as variable rate debt. As both are exceedingly rare in New York State, they shall not be further discussed here.

The State Comptroller has also promulgated rules in conformance with the state administrative procedure act governing the sale of bonds and notes on a negotiated basis. No bond or note sale on a negotiated basis can be conducted by a municipality, school district or district cooperation without prior approval of the State Comptroller except as provided in such rules, which set forth the circumstances under which such approval shall not be required, which includes bonds sold pursuant to the authority specified in Section 63.00 of the LFL.

Bonds may also be sold at private sale to the United States government or any agency or instrumentality thereof such as the U.S. Department of Agriculture (formerly known as the Farmers Home Administration bond program, now referred to as “Rural Development”), the State of New York Municipal Bond Bank Agency, to any sinking fund or pension fund of an issuer selling such bonds, or, in the case of bonds or other obligations of a municipality issued for the construction of any sewage treatment or collecting system, storm water collecting system, water management facility, air pollution control facility or solid waste disposal facility, to the

New York State Environmental Facilities Corporation (which has an interest subsidy program for qualifying issuers and projects) and in certain cases for school districts and some libraries to the Dormitory Authority of the State of New York.

Private Competitive Sale of Bonds

Serial bond issues of under five million dollars (one million dollars on and after June 1, 2012) may also be sold at private competitive sale. This is a hybrid category. What distinguishes it from sales pursuant to Section 57.00 of the LFL as described above is (1) no filing of a debt statement with the State Comptroller is required, (2) no notice of sale need be published, and (3) an official statement will not generally be necessary. It is thus an inexpensive way to sell certain debt by mailed or other transmitted-only notice.

Sales and Closings

Except in the cases of the local placement of notes, small serial bond issues or SIBs, most significant local government debt is sold nowadays in the State and national capital markets with the assistance of a financial advisory firm and bond counsel. Competitive bidding procedures typically are conducted by the financial advisors with legal guidance by bond counsel who drafts the notice of sale and the award documentation. After the award, bond counsel drafts the closing documents, the obligations themselves, and a detailed letter of instruction which is typically forwarded to local counsel, or on advice of counsel, directly to the mutual client. In negotiated note or bond offering, an opinion of local counsel as to any material litigation is often required in addition to the validity opinion of bond counsel. Nowadays, these competitive sales of notes and bonds typically "close" without a formal physical closing (or lunch at a nearby bistro) at a law office. Instead, the issuer forwards the debt obligations themselves to bond counsel or to a national repository on their instruction, and the closing papers to bond counsel. At closing, the purchaser wires the purchase price to the issuer's bank and upon telephonic or facsimile confirmation of receipt, bond counsel, the financial advisor and the purchaser call the repository and "release" the debt obligations to the purchaser. The closing is now complete and all parties may eat lunch at their desks.

CHAPTER TWELVE

Federal Tax Law Issues—Arbitrage and Arbitrage Rebate

The Federal Tax Exemption

Bonds and notes of state and local governmental units generally bear interest that is excludable from gross income for federal income tax purposes for their holders. This federal provision has provided several generations of low-interest borrowings for several generations of local governmental capital improvements. Prior to 1986, the federal government did not ask for much in return. Municipalities and school districts issued this debt, and invested the proceeds until they needed the money for the project. The Internal Revenue Code of the time had some basic rules but they were such that municipalities and schools hardly needed to concern themselves with any federal tax implications of their borrowings, so they didn't. The debt your Affiliated Entity issues on your behalf (or a mortgage note of the Library District itself) will be subject to these post-1985 rules so you need to know about them and you will need to work with your Affiliated Entity to protect the tax-exempt status of debt issued on your behalf. (Free association library debt issued through a local Industrial Development Agency or the Dormitory Authority is subject while a mortgage note of same is not.)

The Tax Reform Act of 1986

On October 22, 1986, the Tax Reform Act of 1986 (the "1986 Act") was signed into law ushering in a new era for tax-exempt finance, and instituting the new Internal Revenue Code of 1986 (the "1986 Code"). The 1986 Code imposed many new restrictions on the ability of state and local governmental units to finance their facilities and operating expenses on a federally tax-exempt basis. For the first time, municipalities and school districts might need to employ taxable financing for some operations that had traditionally been thought of as governmental in nature. In addition to raising the interest cost of borrowing, the 1986 Code increased the administrative burdens placed on state and local political subdivisions in maintaining compliance with the rules relating to tax-exempt financing, thereby further increasing the overall costs of transactions. The 1986 Act could be said to have been a congressional attempt to micromanage tax-exempt debt issuance.

The 1986 Code changed the rules relating to tax-exempt financing in two major ways. First, it sought to eliminate the "arbitrage" profits that at least in the past were frequently generated in tax-exempt financings as a result of an issuer's ability to borrow at low tax-exempt interest rates and invest the proceeds of the borrowing at higher taxable rates until use. Second, it was designed to drastically reduce the ability of state and local governments to undertake tax-exempt financings which benefit nongovernmental entities, regardless of whether the conferring of such benefits is a primary goal or is merely incidental to a true municipal purpose (as would be necessary of a school district or municipal capital project under state law).

Under the 1986 Code a distinction is made between "governmental bonds" and "private activity bonds." A brief discussion of the treatment of private activity bonds under the 1986 Code is included in the next chapter, and should be reviewed with some care, as the terms "governmental bonds" and "private activity bonds" are something of misnomers. For example, obligations issued for a number of legitimate governmental purposes in accordance with state statutory and constitutional requirements may, in some instances, be private activity bonds under the 1986 Code. Unless specifically noted, the restrictions imposed by the 1986 Code apply equally to bond and notes (and to other evidences of municipal indebtedness, as well). Accordingly, as used herein, the term "bond" includes notes (and other evidences of municipal indebtedness).

This chapter will outline those substantive provisions of the 1986 Code that have the greatest impact on issuers of general obligation bonds and notes. Since the vast majority of general obligations issued by school districts and municipalities within New York State would be considered "governmental bonds" under the new law, the discussion of "private activity bonds" has been relegated to the next chapter. Except as discussed in such section, and as may be specifically noted elsewhere, all general obligation bonds and notes issued by a school district or municipality pursuant to the LFL and Article 8 of the State Constitution will be considered to be "governmental bonds" under the 1986 Code.

Arbitrage Restrictions With Respect To "New Money" Issues

Perhaps the most important impact of the 1986 Code on issuers of general obligations like school districts or municipalities is the limitation that it imposes upon the amount of "arbitrage" that the issuer can realize as a result of issuing its obligations at a low tax-exempt interest rate and investing the proceeds of such borrowings in taxable obligations bearing higher interest rates. By taking advantage of this spread between tax-exempt and taxable interest rates, municipalities and school districts in the past could realize arbitrage profits within the fairly liberal constraints imposed by Section 103 of the Internal Revenue Code of 1954 (the "1954 Code") and the Treasury Regulations promulgated thereunder. In addition to being used to pay the costs of issuance of obligations, arbitrage profits often played a key part in the financing of municipal or school district projects.

The 1986 Code accomplishes the goal of limiting the amount of arbitrage profits that a municipality or school district can earn in one major new way. While it generally does not shorten the currently available "temporary periods" during which proceeds of an issue of school district or municipal obligations can be invested in taxable securities with a yield higher than the yield on the bonds, it does require the issuer to rebate to the Federal Government *all* of the arbitrage profits earned with respect to the financing unless all (or in some cases, almost all) of the, original and investment proceeds of the bonds (and, in certain cases, other amounts) are spent within certain set time periods after the date of issuance. It should be emphasized that failure to satisfy this requirement may result in the bonds being retroactively taxable as of their date of issuance.

In addition, the 1986 Code generally prohibits tax-exempt bonds from being issued too far in advance of the time proceeds are expected to be used to construct or acquire the assets to be financed (the so-called "hedge bonds" rule). The temporary period rules and the arbitrage rebate exceptions described in this chapter often provide good reason to issue bonds close to the time when the bond proceeds will be spent; similarly, economics dictates this result whenever the short-term interest rates at which bond proceeds may be invested prior to use are lower than the long term rates at which the bonds accrue interest. However, under certain circumstances, a school district may be interested in issuing bonds at the earliest opportunity. In general, interest on the bonds will not be tax-exempt unless the school district reasonably expects either (i) to spend at least 85% of the net sale proceeds within three years of the date the bonds are issued, as well as invest no more than 50% of the bond proceeds in investments of guaranteed yield of four or more years or (ii) to spend at least 10% of the net sale proceeds within one year, 30% within two years, 60% within three years, and 85% within five years of the date the bonds are issued. These expenditure requirements do not apply to refundings, or to new money bonds in which virtually all of the proceeds of the bonds are invested in other tax-exempt bonds until such proceeds are expended. These hedge bond rules are separate from the arbitrage rebate rule and its exceptions.

Temporary Periods and the "Minor Portion"

The 1954 Code, as amended up to 1986, provided "temporary periods" during which the proceeds of an issue of municipal or school district obligations could be invested in taxable obligations having a yield which exceeded the yield on the bonds. In the case of obligations issued for construction or acquisition, a three-year temporary period was generally available. In the case of cashflow borrowings, such as revenue anticipation notes, tax anticipation notes, and grant anticipation notes (*e.g.*, bond anticipation notes issued to refund the portion of the costs of a project anticipated to be paid with Federal or State grants-in-aid) a temporary period of at least thirteen (13) months has been generally available if the proceeds of the issue did not exceed the "maximum anticipated cumulative cashflow deficit" that was expected to occur during the term of the borrowing.

The 1986 Code does not reduce these temporary periods. However, for all bonds and notes, the former "minor portion" rule, under which up to 15% of the bond proceeds could be invested at an unrestricted yield even after the expiration of the applicable temporary period, was replaced with a new minor portion rule. The "minor portion" is now limited to the lesser of 5% of bond or note proceeds or $100,000.

The new "minor portion" is in addition to any proceeds deposited in a reasonably required reserve fund. However, while a reasonably required reserve fund can also generally be invested without restriction as to yield, the amount of original bond proceeds which can be deposited in such a fund is limited to 10% of bond proceeds. Moreover, even if cash on hand is used to fund a larger reserve, the amount held in the reserve that may be invested at an unrestricted yield is still limited to 10% of the original bond proceeds. Thus, any amounts held in a reserve fund that are in excess of 10% of the original bond proceeds must be yield restricted. There are, however, exceptions to these 10% limitations for issues which the Treasury Department determines require a larger reserve fund. (In New York, it is generally not permissible to fund the type of reserve fund addressed here with the proceeds of general obligations, so this is not discussed further.)

Definition of "Yield"

The 1986 Code substantially revises the definition of "yield" by legislatively overruling then current case law. Under the new law, yield must now be calculated based on the price at which the obligations were-sold to the public, rather than the funds received by the issuer after the payment of underwriter's compensation and other issuance costs. This has the effect of reducing the yield on the bonds, thus decreasing the permissible arbitrage profit which may be earned (although subject to rebate) after expiration of the applicable temporary period. In many cases, "negative arbitrage" will result. In effect, unlike prior law, issuance costs can no longer be partially "recovered" from arbitrage earnings.

The 1986 Code does, however, provide that certain credit enhancement fees, such as municipal bond insurance premiums and letter of credit fees, may be treated as interest payments on the bonds if such fees result in a net present value interest savings to the issuer. By treating these payments as interest on the bonds, the "yield" on an issue is increased, thereby allowing bond proceeds to be invested at a correspondingly higher yield with the result that the issuer can recoup a portion of such credit enhancement fees from permissible arbitrage.

In all circumstances where yield restrictions are imposed, the issuer is obligated to abide by the "market price rules." Thus, an issuer cannot artificially limit its apparent yield by investing in obligations which bear a below-the-market interest rate or by acquiring an investment at a price in excess of its fair market value or selling it at a price below its fair market value. When yield must be restricted and there is no suitable investment available in an arms-length transaction, an issuer can subscribe for United States Treasury Securities—State and Local Government Series (commonly referred to as "SLGS"), which are United States Treasury Bonds, Notes or Certificates of Indebtedness with yields and terms tailored to the school district or municipality's needs which are sold by the United States Government to municipalities or school districts and states. In the alternative, the municipality or school district can invest in tax-exempt obligations (subject, of course, to the limitations set forth in Section 165.00 of the LFL). The Treasury Department was mandated by the 1986 Act to develop a "money market"-type, flexible SLGS program to accommodate issuers.

Rebate Requirement and Exceptions

The General Rule. Even if arbitrage profits are permissibly earned, in the first instance, pursuant to the exceptions for temporary periods, the minor portion and reasonably required reserve funds, the issuer must nevertheless rebate to the Federal Government *all* the arbitrage profits that are earned from the date of issuance of the bonds. (See below for *de minimus* exceptions to the rebate requirement that apply when *all* original and investment proceeds of the obligations are spent within six months of their date of issuance.) The amount which must be rebated to the Federal Government is equal to only the arbitrage "profit" that results from the investments. For example, if a municipality issued tax-exempt 30-year bonds having a yield of 8% and earned 10% on its investments, only those earnings attributable to the difference between 10% and 8% would have to be rebated. The rebated amounts must be paid to the Internal Revenue Service at least every 5 years and within 60 days of the date that the last of the bonds is retired. In effect, this renders useless temporary periods and minor portions since issuers will have to rebate most of the profits they have earned in any event.

Rebate cannot be avoided by investments that violate the previously discussed "market price rules." However, where feasible, investment in tax-exempt obligations is an alternative to avoid rebate. (However, an issue may permissibly utilize demand deposit accounts (such as N.O.W. Accounts) rather than investing proceeds in certificates of deposit, treasury Bonds, Bills or Notes, or other high yielding types of investments, so long as the investment is made in accordance with the "market price rules," and complies with other limitations applicable to investments of proceeds by the issuer (*e.g.*, those found in the Local Finance Law, or General Municipal Law).) Note that the restrictions of LFL Section 165.00 apply to proceeds of all types of obligations except tax anticipation notes and revenue anticipation notes.

The provisions of Section 11 of the General Municipal Law apply to investments of proceeds of TANs and RANs. Simply placing proceeds in a noninterest bearing account (such as a typical checking account) will not obviate the necessity to make a rebate. Since the bank is gaining the use of those funds at no cost, an interest rate would be imputed by the IRS for the deposit.

Arbitrage Rebate and its Exceptions

Since the effective date of the 1986 Code, all school districts (and other municipalities such as counties, towns, villages and cities) have been potentially subject to the arbitrage rebate rules whenever they issue federally tax-exempt bond anticipation notes, capital notes, statutory installment bonds or other serial bonds for capital projects. These rules, in the form of detailed

U.S. Treasury regulations, can require school districts to pay to the federal government much of the interest earnings on proceeds received by the school district from the issuance of such tax-exempt obligations and invested prior to use for their intended purposes.

However, the Code and regulations do provide several exceptions to these generally applicable rules:

1. an exception for governmental issuers, such as counties, cities, towns, villages, fire districts and school districts, who do not reasonably expect to issue more than $5,000,000 in tax-exempt obligations in the current calendar year (this is the so-called "small issuer" exception);
2. an exception *solely applicable to school districts* who, in addition to the issuance of not to exceed $5,000,000 in tax-exempt obligations for any school district purpose (i.e., cashflow or capital) in the current calendar year (as noted in (1) above), do not reasonably expect to issue more than an *additional* $10,000,000 in tax-exempt obligations in the current calendar year, *provided*, such additional $10,000,000 (or such lesser amount as is applicable if the school district is not issuing that much) is attributable *solely* to financing the "construction" of "public school facilities" (the "school small issuer" exception not generally applicable to school districts but is included here in the interests of completeness).
3. an exception for governmental issuers of RANs or TANs, regardless of whether they reasonably expect to issue more than $5,000,000/$15,000,000 in the current calendar year, if the issuer can meet certain rapid spend-down requirements once the obligation is issued; and
4. several exceptions for governmental issuers of notes or bonds for capital projects regardless of whether they reasonably expect to issue more than $5,000,000/$15,000,000 in the current calendar year, if the issuer can meet certain rapid spend-down requirements once the obligation is issued.

Small Issuer Exception to Rebate Rule. *This exemption from the rebate requirement is for governmental bonds or notes issued by small governmental units with general taxing powers which will not issue in excess of $5/$15 million of governmental obligations in any given calendar year. This exemption does not apply to the first $5/$15 million of issues of governmental units which will issue more than $5/$15 million per year. The issues of any "subordinate" governmental issuers must be aggregated with the issues of an issuer for purposes of the $5/$15 million limit.*

For purposes of this requirement, an entity will be deemed "subordinate" to the issuing governmental unit if the entity derives its power to issue obligations from the governmental unit or is subject to substantial control by the governmental unit. However, the mere fact that the entity is located within the boundaries of the issuing governmental unit will not, in and of itself, be viewed as making the entity "subordinate" to the governmental unit. (This aggregation requirement is generally unimportant for New York issuers, since it requires aggregation only of issues by subordinate entities which derive their power to issue indebtedness from the entity in question. Geographic location within the territory of an issuer does not mean that one municipality is subordinate. However, issuance by an urban renewal agency, for example, would probably have to be aggregated with the issuances of the municipality to which it relates.)

If your School District may be a "small issuer" in any current calendar year in which general obligation notes or bonds are proposed to be issued, there is a three-step analysis which must be completed to confirm that status:

Step No. 1: Determine whether the school district or municipality reasonably expects to issue an aggregate of $5,000,000 or less in tax-exempt notes or bonds in the calendar year.

WHAT COUNTS:

1. All new money governmental issues (BANs, Serial Bonds, RANs, TANs, Capital Notes), including those issued for the benefit of the Library District.
2. Advance refundings (renewal of a note or bond more than 90 days in advance of its maturity or redemption date).
3. All governmental new money or advance refunding bonds or notes issued by a governmental entity subordinate to the municipality or an entity issuing "on behalf of" same (i.e., certain I.D.A. debt may count).
4. All tax-exempt lease purchase or installment sales agreements.

WHAT DOES NOT COUNT:

1. Current renewals (to the extent that the amount of the renewal does not exceed outstanding principal amount of maturing debt, i.e., typical bond anticipation renewal notes).
2. Private activity bonds or notes (i.e., obligations, the proceeds of which are used for a capital project with a private business user receiving some substantive benefit from the project).
3. Most federally taxable debt obligations.

Step No. 2: Determine whether, in addition to the obligations considered in Step No. 1, the school district reasonably expects to issue an additional amount, not to exceed $10,000,000, for public school facilities construction costs. (In effect, this means that no more than $5,000,000 in a calendar year can be new money tax or revenue anticipation note borrowings.) This is likely often for a School District in this state.

Note that for Steps No. 1 and No. 2, this is a "reasonable expectations" standard which the school district must apply to itself at the time of each borrowing. The expectation of being and remaining a "small issuer" is not made one time for each calendar year. It is made each time the school district proposes to borrow. Likewise, an unanticipated borrowing later in a calendar year which unexpectedly brings an issuer over the $5,000,000/$15,000,000 mark does not "taint" debt previously issued in that calendar year, and thus does not make such prior debt retroactively subject to the arbitrage rebate rules.

Step No. 3: Determine whether the particular note or bond issue itself is eligible for the "small issuer" exceptions to the general arbitrage rebate requirement. The fact that the school district has determined in Step No. 1 (and Step No. 2, if applicable) that it is, indeed, a "small issuer" does *not* automatically exempt its note or bond issue from the rebate requirement. The note or bond issue itself must also meet certain requirements:

A. NEW MONEY ISSUES

1. 95% or more of net proceeds of the issue are to be used for local governmental activities of the issuer.
2. Not a "private activity" bond or note (i.e., proceeds not used for a capital project with a significant private business user of the project).

B. RENEWAL/REFUNDING ISSUES (current or advance)

1. Aggregate face amount does not exceed $5,000,000/$15,000,000.
2. Each refunded bond or renewed note was part of an issue which itself qualified at the time for the "small issuer" exception in its year of issuance.
3. The average maturity date of the refunding/renewal obligation is not later than the average maturity date of the obligations being refunded/renewed.
   Note: This rule in itself would eliminate renewal notes or bonds from qualifying when refunding/renewing typical one year notes so there is an exception:
   If the average maturity of the refunded debt is three years or less, the requirement is waived. (School District or municipality debt most frequently renewed is in the form of one year or less bond anticipation notes; these qualify for this waiver.)
4. No refunding bond can have a maturity date which is later than the date which is 30 years after the date that the original note or bond was issued.

NOTE: it is possible to be a $5,000,000 or under "small issuer" (or a $15,000,000 or under "school small issuer"), and still be required to rebate if the issue itself does not meet the requirements of step no. 3.

C. COMBINATION NEW MONEY/RENEWAL-REFUNDING ISSUES

1. All of the above-stated rules apply.
2. The aggregate face amount rule may require that a consolidated issue be split into two issues.

6-Month/12-Month Exception to Rebate Requirement: Under a special exception to the rebate rule, no rebate will be required if all of the original and investment proceeds of the issue, except for a "minor portion" equal to the lesser of 5% of the bond proceeds or $100,000, are expended within six (6) months of the date of issuance of the obligations, and all of the proceeds, including that "minor portion," are spent within twelve (12) months of the date of issuance. However, this rule does not apply to revenue anticipation note and tax anticipation note issues ("RANs" and "TANs," respectively), which have a separate exception noted below.

This 6-month/12-month exception to rebate requirement must be considered in conjunction with Section 165.00 of the LFL which limits the use by New York issuers of investment proceeds to the payment of debt service on the municipal obligations with respect to which such amounts constitute proceeds. In the case of notes, unless all proceeds are expended *immediately*, there will be at least some investment earnings which cannot be expended to pay debt service until the maturity of notes. Thus, unless the maturity of notes is limited to 6 months or less, an issuer will not be able to avoid the rebate requirement under the 6 month/12 month exception unless all original and investment proceeds in excess of the "minor portion" (i.e. all such proceeds in excess of the lesser of 5% of the proceeds or $100,000) are expended within the first 6 months and the minor portion is spent within the second six (6) months, thus, if the "major portion" proceeds (i.e. all proceeds except that amount which is the lesser of 5% or $100,000) cannot be expended within the first six (6) months, or if only a minor portion remains unexpended as of such date but such minor portion cannot be expended within the second six (6) months, then all the arbitrage must be rebated. Where an issuer expends a "major portion" of the proceeds of its issue within six (6) months and uses the entire remaining "minor portion" to pay debt service within the next six (6) months, the necessity to make any rebate will be avoided.

Six-Month Exception for RANs and TANs: A separate exception to the rebate requirement is available for RANs and TANs. First, in order to be exempt from the rebate requirement, *all* of the original and investment proceeds of the RANs or TANs must be spent within the first six months. Second, there is a special rule for determining whether all of the proceeds of RANs and TANS will be deemed to have been expended within the first six months. The rule states that the original and investment proceeds of such issues will be treated as expended on the first day after the date of issuance that the *actual* cumulative cashflow deficit exceeds 90% of the issue's face amount. In this calculation, all other proceeds available for the governmental purpose of the borrowing must be treated as spent first, with the result that the original and investment proceeds of the RANs or TANS are viewed as having been expended last. For this purpose (unlike the method for determining the maximum permissible size of the issue which remains the same as under prior law), no allowance is permitted for a working cash balance equal to the issuer's estimate of an additional month's gross expenditures and the deficit is calculated on the basis of actual experience. Thus, the allowance for a working cash balance remains available for sizing issues but its inclusion in the face amount of a financing could make it difficult to meet the safe harbor test. This means that some issuers should probably reduce the size of their RAN and TAN issues so as to assure that all of the proceeds will be viewed as expended within six months in order to avoid rebate. This may necessitate a schedule of semiannual RAN and TAN borrowings with maximum cashflow deficits projected to occur within six months. RANs and TANs should benefit from the rebate exception for bona fide debt service funds (discussed below) as regards their LFL Section 25.00(g) and 24.00(e) funds. *See* Chapter 8.

The Six Month Capital Spend-down Exception: an exception for all local governmental issues, including school districts, which actually spend all of the borrowed process (and investment earnings thereon) for a capital project on or before the date six months after the closing date for the new money notes or bonds (exception for an amount not to exceed 5% of the proceeds of such issue, as long as such amount is spent no later from an additional six months thereafter.) This exception is *not* limited to construction and reconstruction projects, and is likely to be most useful in acquisition financings, reimbursement financings and current refundings.

The 18-month Capital Spend-down Exception: an exception for all local governmental issuers, including school districts, which actually spend all of the borrowed proceeds (and investment earnings thereon) for a capital project in accordance with the following schedule: at least 15% with six months, at least 60% within twelve (12) months, and 100% within eighteen (18) months (in each case, measured from the date of issuance) except that an amount held for reasonable retainage after eighteen (18) months is permitted as long as it is expended for the capital project within thirty (30) months of the issue date. This exception is *not* limited to construction and reconstruction projects.

The 2-Year Construction Spend-down Election/Exception: an exception for all local governmental issuers of notes or bonds, including school districts, for capital construction and reconstruction projects only regardless of whether they reasonably expect to issue more than $5,000,000 in the current calendar year, if the issuer can meet certain rapid spend-down requirements once the obligation is issued. The rules for this much-utilized exception are as follows:

How to Calculate the Construction Spend-down Election/Exception

Step No. 1: The first step is that the school district or municipality designate the issue as a "*construction issue*" (this can be done where 75% of the proceeds are allocable to construction vs. acquisition; bond or note issues may be bifurcated for this purpose). "Construction issue" is defined in the Internal Revenue Code of 1986, as amended to include reconstruction and rehabilitation expenses. A "construction issue" is entitled to avoid arbitrage rebate if the school district or municipality can meet certain spending rules which are much more favorable than the "95% in the first six months—5% in the next six months" schedule which is available for acquisitions. The spending rules for a designated construction issue give the school district or municipality the following schedule: The school district or municipality would have to expend 10% of the proceeds, including earnings on investments, within six months of the date of issuance of the obligations; 45% of the proceeds, including earnings on investments, within twelve months of the date of issuance of the obligations; 75% of the proceeds, including earnings on investments, within eighteen months of the date of issuance of the obligations; and 100% of the proceeds*, including all remaining earnings on investments, within two years of the date of issuance of the obligations unless a retainage is required by law, in which event, the 100% becomes 95% and the final 5%, including all remaining earnings on investments, must be expended within three years of the date of issuance of the obligation. (Money is expended only when the check is not only written but also delivered.)

Step No. 2: The second step of the "*construction issue*" designation process is that the school district or municipality must elect whether the bond or note issue should operate under the so-called "Penalty Option" or decline to operate under such "Penalty Option." If the school district or municipality elects to operate under the "Penalty Option," then failure to meet any of the spending tests at the six-month expiration, the twelve-month expiration, the eighteen-month expiration, the two-year expiration or the three-year expiration, will subject the school district or municipality to a penalty instead of arbitrage rebate for that particular period. The penalty is calculated by multiplying the difference between what the school district or municipality did spend and what the school district or municipality should have spent by 1.5% and this will give the school district the amount that the school district or municipality has to pay as a penalty to the federal government for that period.

For instance, if a school district or municipality had to expend $100,000 within the first six months and the school district or municipality only expended $90,000 as of that date, the difference, $10,000, would be multiplied by 1.5% which produces $150.00 and this $150.00 the school district or municipality would have to pay to the federal government.

The advantage of the "Penalty Option" is that the penalties are a lot easier to calculate than the arbitrage rebate. However, for the reason described below, it is rarely chosen.

On many occasions (for instance, during a period of "negative arbitrage") a school district or municipality may not wish to elect the Penalty Option. In this case, the school district or municipality would designate the issue as a "*construction issue*," but the school district or municipality would specifically decline to elect the penalty option. In such case, it would still be subject to the same 10%–six months; 45%–12 months; 75%–18 months; 100%–2 years (or 95%–2 years with remaining 5%–3 years) spending tests, but if the school district or municipality should fail to meet such spending test, then the school district or municipality would not owe the aforesaid 1.5% penalty; rather, it would be subject to rebate on the investment (arbitrage) earnings, *BUT ONLY* to the extent the school district or municipality had such earnings; *and* such earnings exceeded the overall arbitrage yield on the bond or note issue. This makes the most sense at those common times when the school district or municipality expects to spend the proceeds quickly and reinvestment rates are relatively low compared to the rate the school district or municipality is paying on an issue. In such event, the school district or municipality may not even be able to earn any arbitrage earnings to rebate in the first place, or may well earn less than the amount which the penalty would be. In such "negative arbitrage" or similar situations, it may not make sense to elect to pay a penalty when investment earnings would not be rebatable because they do not exist (or they would be less than the penalty amount(s)).

Bona Fide Debt Service Fund Exception to Rebate Rule. There is one other special rule regarding exemptions from the rebate requirement for any issue with a maturity of less than five years such as BANs, BARNs, RANs and TANs. Any amount earned on a "bona fide debt service fund" will not be taken into account in determining the aggregate amount to be rebated for a given year if the gross earnings on such fund for any bond year are less than $100,000. In the current interest environment, this means that fairly substantial debt service funds can still earn arbitrage without rebate. This includes such funds established for RANs or TANs under LFL Sections 25.00(g) and 24.00(e). In addition, arbitrage earnings in such a fund are exempt from any rebate payment for most issues of bonds that have a fixed rate of interest or for issues with an average annual debt service of $2,500,000 or less.

Administrative Burdens. In addition to eliminating most, if not all of the arbitrage profits that may presently be realized by municipal issuers of tax-exempt obligations, the rebate requirement necessitates burdensome new accounting procedures and may' require complex mathematical computations that are beyond the capability of all except the most sophisticated financial managers. Since failure to satisfy the rebate requirement may result in the bonds becoming taxable as of their date of issuance if the failure is due to "willful neglect" (or in the imposition of an additional penalty of up to 50% of the amount of the issuer failed to rebate, even if the failure is due to "reasonable cause"), it seems obvious that many school districts will be forced to retain accountants or others to perform this task, thus further increasing the total costs for the bond issue.

Reasonable Expectations. Under the 1954 Code, if an issuer did not reasonably expect to invest the proceeds of the tax-exempt obligations in taxable obligations with a yield materially higher than the yield on the bonds (except for permitted temporary periods, minor portions and reserve funds), then a certification to that effect served to protect the tax-exempt status of the bonds. The 1986 Code clarifies this "reasonable expectations" test by providing that any subsequent "intentional" act which produces arbitrage after the bonds are issued will render the bonds taxable retroactively to their date of issuance.

Summary. The net result of the new rules relating to the reduced minor portion and the redefinition of "yield" is that issuers will be able to *earn* lesser amounts of arbitrage in the first instance than has previously been the case. Moreover, if the obligations do not qualify under the "small issuer" exception, and all proceeds of the issue are not-spent within six months (except, in the case of obligations other than RANs or TANs, for the lesser of 5% or $100,000 which is allowed to remain invested for a year if the rest of the proceeds are spent within-six-months), any arbitrage profits that issuers *do* earn will have to be rebated to the Federal Government. More frequent issuance at greater cost seems the most likely practical solution. Issuers will also have to be more vigilant to ensure that they do not violate the arbitrage rules so that the tax-exempt status of their obligations is not put at risk.

Restrictions on Refundings. The 1986 Code also applies severe new restrictions on the current ability of municipalities to advance refund their existing tax-exempt indebtedness. The new law defines an "advance refunding" to be a refunding transaction where the refunding obligations are issued more than ninety (90) days prior to the repayment of the refunded obligations.

It is extremely rare for bond anticipation renewal notes to be issued other than simultaneously with the maturity of the outstanding notes of which they are renewals. When renewal notes are issued before the maturity of the refunded notes, it typically is only done one or two days prior to the maturity of the outstanding notes, and then only for the convenience of the issuer. Thus, most renewal note issues are "current" refundings, not subject to the advance refundings rules. On the other hand, serial bonds are often issued for the purpose of refunding several series of notes, with the result that some of the refunded notes are redeemed more than 90 days after the issuance of the serial bonds.

If the refunded notes were issued after August 15, 1986, any portion of the temporary period remaining for the unexpended proceeds of the refunded notes terminates upon. The date of issuance of advance refunding obligations and such remaining proceeds must then be invested at-a yield no higher than the yield on the refunded obligations plus 1/8 of one percent until the refunded notes are paid. After such date, such proceeds can be invested at a yield no higher than the yield on the refunding obligations. For other refundings (*i.e.*, so-called "current" refundings), the balance of any remaining temporary period for proceeds of the refunded obligations remains available. In all cases, the proceeds of the refunding issue may be invested only in accordance with the rules described in the text.

In connection with refundings, note that, to the extent that unexpended proceeds of an original borrowing (and the interest earnings thereon) remain when an issue of obligations is refunded, such proceeds are considered to be "transferred proceeds" of the refunding issue as of the date on which the proceeds of the refunding issue are used to pay off the refunded issue. Where the outstanding obligations being refunded were issued prior to August 16, 1986, any remaining proceeds of such obligations will be unaffected by the 1986 Code until, and unless, refunding obligations are issued. At the time such proceeds become transferred proceeds of the refunding issue, they are subject to the arbitrage rebate rules outlined above in the text, and (assuming the refunding issue (or an issue which it refunded) was originally issued more than six months prior to the date on which such proceeds become transferred proceeds) the issuer will be obligated under the 1986 Code to rebate to the Federal Government all arbitrage profits realized after they become transferred proceeds, which will require valuation of all assets in which such proceeds are invested as of such date.

Governmental bonds may be advance refunded only if *all* of the following conditions are satisfied:

a. Bonds or notes originally issued before January 1, 1986 may not be advance refunded more than twice (or, if already advance refunded twice before March 15, 1986, not more than once after such date). Thus, for example, if a School District issued "new money" BANs in 1983, issued refunding BANs in 1984 more than 180 days prior to the maturity of the 1983 BANS, and issued refunding bonds in February of 1985 to refund the 1984 BANs more than 180 days prior to their maturity date, the bonds could only be advance refunded one more time.

b. Bonds or notes originally issued after December 31, 1985 can only be advance refunded once.

In the case of refunded bonds or notes issued after 1985, the refunded obligations must be called on the first call date if there are (or may be) present value debt service savings (determined without regard to administrative expenses) as a result of the refunding.

In the case of refunded bonds or notes issued before 1986 (most of these will have already matured in full), the refunded obligations must be redeemed at the earliest date on which they can be redeemed at par or at a premium of 3% or less if present value debt service savings will (or may) result from the refunding.

The original and investment proceeds of the advance refunding bonds are granted a temporary period of only 30 days. At the end of such temporary period, the proceeds of the refunding bonds can be invested at a yield no higher than the yield on the bonds (plus a truly *de minimus* amount known in the business as "the peanut"). It is important to note that the temporary period rules and the arbitrage rebate rules are independent. Thus, even if a temporary period is available, if all proceeds of an issue, including a refunding issue, are not expended within six months (subject to the "minor portion" exception discussed above), arbitrage profits, including profits earned during a temporary period, must be rebated. In the case of refundings, issuers must exercise particular care to insure that not only the refunding bond proceeds are promptly expended, but also that the refunded bond proceeds were spent within six months. Moreover, any remaining temporary period with respect to unexpended proceeds of the refunded obligations terminates as of the date of issuance of the refunding obligations if the refunded obligations were issued after August 15, 1986. Thus, as of the date of issuance of the refunding bonds, all unexpended proceeds of such refunded obligations must be invested at a yield no higher than the yield on the refunded obligations (plus 1/8 of 1%). This, of course, would be very detrimental to the issuer where bond anticipation notes, or other short-term municipal obligations bearing a very low interest rate, are refunded more than 90 days prior to their maturity. Moreover, as of the date the refunded obligations are actually paid off, any remaining proceeds of the refunded obligations must be invested at a yield no higher than the yield on the refunding obligations (plus 1/8 of 1%).

The minor portion for the refunded obligations must be reduced on the date of issuance of the refunding bonds to an amount no greater than the lesser of 5% of the refunded bonds' original amount or $100,000.

If the refunded obligations were issued after August 15, 1986 or if the refunded obligations were issued to finance an "output" facility (i.e., on electric generation or gas facility, but not a water facility), an advance refunding issue will require "volume cap" to the extent of any private use of the proceeds of the refunded bonds that exceeded $15 million, with such use determined as of the date of issuance of the refunded bonds. However, unanticipated changes in use must also be taken into account; therefore, total private use of the refunded bond proceeds must be considered.

Information Reporting Requirement

In order for its obligations to qualify for tax-exemption, the issuer must file with the Internal Revenue Service an information return with respect to *all* obligations The return, similar to the Form 8038 required only for certain nongovernmental bonds under earlier law, requires information relative to, among other things, the issuer, the bonds (including the date of issuance, amount of net proceeds, interest rate, costs of issuance and the amount of any reserves), and, where applicable, any private users of the bond or note proceeds. Failure to file this return will cause interest on the bonds or notes to be taxable as of the date of issuance unless relief is sought from, and granted by, the Internal Revenue Service.

CHAPTER THIRTEEN

Federal Tax Law Issues—Private Business Use of Library District Financed Facilities

Introduction

Federal tax law governing local governmental issuance of tax-exempt debt includes a concern with private business beneficiaries of such tax-exempt financing. At the outset, it is necessary to remind ourselves: so does the Constitution and applicable statutes of the State. Indeed, assuming a Library District is in compliance with State laws governing private use of government facilities and resources such as the loan of credit and valid purposes provisions of the Constitution described in an earlier chapter, and the implementing statutes, case law, and opinions of the office of the State Comptroller, compliance with the federal tax law rules in this area is very likely. Nevertheless, a review of the tax rules is appropriate since the debt issued by your Affiliated Entity on your behalf will be subject to them and this may have an impact on you.

Federal Restrictions on Tax-Exempt Financing for the Benefit of Nongovernmental Entities Before 1986

Before the 1986 Code, up to 25% of the proceeds of tax-exempt municipal obligations could be "used" for the benefit of taxable business entities. However, the indirect, as well as the direct, use of bond proceeds had to be taken into account for purposes of determining whether the 25% limitation was exceeded. Thus, for example, the lease of all or a portion of a bond-financed facility to a taxable business entity was treated as an indirect use of the bond proceeds by such entity. Therefore, prior to the 1986 Code and if permissible under State Law, a municipality could issue tax-exempt obligations to finance an office building and lease up to 25% of the office space to one or more taxable business entities without impairing the tax-exempt status of the bonds. (This would not be permissible in New York State.) However, if more than 25% of the building were leased to such entities, more than 25% of the bond proceeds would be viewed as being indirectly "used" by such entities and, thus, the bonds would generally be taxable. A similar rule applied in certain instances where a taxable business entity agreed to operate a bond-financed facility on behalf of a municipality as well as to other arrangements whereby one or more taxable business entities agreed to purchase the output of a bond-financed facility such as, for example, a municipally-owned electric generating plant. (This type of arrangement can be permissible in New York State, subject to many restrictions.)

In addition, tax law prior to 1986 provided that, with certain enumerated exceptions, no more than 5% of the proceeds of an issue of municipal obligations could be "loaned" to persons other than state or local governmental units or certain charitable organizations. However, the 5% threshold for "loans" has not usually presented a problem to issuers of traditional general obligation bonds because the proceeds of such issues cannot typically be loaned to nongovernmental entities under the provisions of our State Constitution noted earlier. Moreover, the 25% limit also had not been a serious problem because the indirect "use" of general obligation bond proceeds by taxable entities is usually *de minimus*, as school districts and municipalities are without authority to do so, in most cases.

Finally, earlier tax law did not require that any nongovernmental use of bond proceeds be related to governmental uses of such proceeds of any particular issue.

Private Activity Bonds Under the 1986 Code

Under the 1986 Code, an issue of municipal obligations is deemed to constitute "private activity bonds," and therefore generally subject to Federal income taxation, if 10% or more of the proceeds of the bonds is "used," directly or indirectly, in the trade or business of persons other than state or local governmental units or members of the general public on an equal basis and if 10% or more of the debt service on the bonds is secured by funds from private users, (e.g., rental payments for the use of bond-financed facilities). "Use" includes leasing a bond-financed facility, purchasing output from a bond-financed facility, or certain management contracts (including such contracts as are permissible in New York State). Debt service will be considered to be "secured" by funds of private-users even if no direct link exists between debt service and moneys paid or available from a private user. Thus, the fact that debt service is paid from moneys in an issuer's general fund is not significant, if moneys are paid by the private user' to the issuer and applied by the issuer for a purpose other than direct payment of the obligations. Continuing the rule of prior tax law, bonds will also be private activity bonds if 5% or more of the bond proceeds or $5,000,000, whichever is less, is "loaned" to persons other than state or local governmental units. (For purposes of these tests, the portion of the bond or note proceeds used by all nongovernmental beneficiaries of the obligations is aggregated. *Note that Section 501(c)(3) charitable organizations are not exempt users of bond proceeds for purposes of the "use" and "loan" provisions. They are, in effect, private, non-governmental users, albeit as noted below, treated significantly more leniently than private business use by a profit corporation and such use permitted if certain regulations are complied with.* The term "loan" is to be broadly construed. The only exception to this 5% or $5,000,000 rule is provided for loans that enable the borrower to finance any governmental tax or assessment of general application for an essential governmental function. Thus, the present ability of state and local governmental units to issue tax-exempt obligations to finance tax assessments or certain types of public improvements, such as water and sewer lines, is not impaired as long as the financing is made available to all members of the general public on an equal basis.

Although the legislative history of the 1986 Code stated that its provisions were not intended to interfere with traditional municipal financings, lowering the threshold from 25% nongovernmental use to 10% can call many more projects into question than was previously the case. Nowadays, a question has to be asked about other users of governmental facilities to be financed; whereas before 1986, it was largely irrelevant for cities, towns, villages, school districts and the like. The following example illustrates these restrictions:

Private Use—Example

A Library District wishes to have issued on its behalf general obligation bonds to finance purchase and reconstruction of an existing empty 3-story building as a new central library and office complex. The building purchase and reconstruction/conversion will cost $5 million. Because the building is located on the edge of a small business district, the Library District desires to lower its overall occupancy costs by leasing out the first floor for use as shops and stores (or as offices for a local charitable organization) temporarily until needed for Library District use. Because of these leases, more than 10% of the bond proceeds will be viewed as being "used" by the store owners or charity and, since the rental payments would be viewed as "securing" the bonds even if they are not formally pledged to the payment of debt service, the bonds will be private activity bonds. The same result would apply if the first floor consisted of a parking spaces for use by the library district and the public if the library district, rather than operating such facilities itself, hired a private management company to perform such function pursuant to certain types of long-term contractual arrangements.

Related Use Rule Under the 1986 Code

The 1986 Code imposed additional requirements even if the new 10% rule is not violated. Under the 1986 Code, if over 5% of the proceeds of a bond issue are used by private entities in a way that is not related to the governmental purpose of the rest of the issue, the bonds become taxable. This provision ended the era of consolidated issues in which private uses were "flooded" as part of large issues in which 75% or more of the proceeds would be used for assorted traditional governmental purposes with the "private" financing being limited to 25%. Now, only 5% of the bond proceeds can be used for the benefit of private entities without any further restrictions. The remainder of the permissible 10% that is used for the benefit of private entities must satisfy two additional restrictions—first, any such additional private financing must be "related" to a governmental facility that is also being financed with the bond issue; second, the amount of bond financing provided to the private entity with respect to such facility cannot exceed the amount of financing being provided to the governmental entity with respect to the same facility.

For example, if a $1,000,000 bond issue were to be used to finance a courthouse costing $900,000 that was to be used solely by a governmental entity and a $100,000 improvement at the issuer's airport, which is used mainly by commercial airlines, the bonds would be taxable even though the 10% limit was not violated because over 5% of the proceeds would be used for an "unrelated" facility. However, if the $100,000 were instead used to finance a privately operated cafeteria located in the courthouse that would be used predominantly by municipal employees, the bonds would be tax-exempt because the additional financing being provided with respect to the cafeteria (i.e. the amount in excess of the 5% unrestricted amount) would be "related" to the governmental use of the facility and the bond-financed cost of the cafeteria does not exceed the amount of financing being provided to the governmental entity with respect to the same facility.

In the case of an issue in which more than 5% of the proceeds, but less than 10%, are to be used for an unrelated purpose, the entire issue would be treated as a private activity bond, requiring a public hearing and becoming subject to the alternative minimum tax. Furthermore, if the private use is not one treated as an exempt purpose under the 1986 Code, there is a risk that the whole issue would be retroactively characterized as taxable (even if 90% of the bonds were used for a traditional governmental purpose).

Because of these stringent requirements and the severe penalty, school districts and municipalities must regularly examine their financing plans very carefully in order to determine whether or not tax-exempt financing is being made available to entities other than state or local governmental units or members of the general public on an equal basis, and should consult with bond counsel early in the planning process if any questions are raised in this regard. *Some* obligations which are private activity bonds *may* still be entitled to tax exemption, but only if they meet all of the applicable requirements of the 1986 Code, including the holding of a public hearing and, in some cases, obtaining an allocation of "volume cap" from the State.

Private Activity Bonds That Qualify For Tax-Exemption as "501(c)(3) Bonds," "Exempt Facility Bonds," "Qualified Redevelopment Bonds" or Small Issue "Industrial Development Bonds"

Although private activity bonds are generally taxable under the 1986 Code, there are several exceptions to this rule that provide at least some relief. Thus, some private activity bonds nevertheless qualify for tax-exempt status if, for example, they constitute "501 (c)(3) bonds" issued to benefit a not-for-profit organization holding that status. (*See* Chapter 22 on the applicable rules.) In addition, "qualified redevelopment bonds" or bonds issued to finance the various types of "exempt facilities," or some types of "industrial development," each under its own qualifying set of conditions can retain tax-exempt status. These permutations are beyond the scope of this primer, as the primer is directed to general obligation governmental bond issues which would not generally finance such facilities or projects.

State Law Aspects of Private Activity

A full review of the basic rules governing non-governmental use of Library District facilities is beyond the scope of this bond primer. In brief, and subject to the specific facts and circumstances in any case, and certain statutory case law, and State Comptroller opinion exceptions, these are the rules in "nutshell" form:

- No gifts or loans of public funds or properties to any private individual, private undertaking, private corporation or association;
- No gifts or loan of credit to same or to any other municipality or school district or library district;
- No contracting indebtedness except for a valid Library District purpose;
- Truly incidental private benefit is permissible;
- Private management contracts negotiated at arms length to operate certain Library District facilities on behalf of a Library District are permissible under certain limited conditions;
- Property leased by a Library District may be improved for Library District use provided that such improvement is completely amortized during the life of the lease;
- A Library District cannot be in the landlord business as an investment but it can acquire a property needed for a valid Library District purpose that is larger than current need as long as the entirety is reasonably expected to be needed by the Library District in the "foreseeable future." Such temporary use by others if at fair market value is permissible but if the property was bond-financed, "private activity" considerations are paramount and should be considered prior to leasing to the private user.
- Please note that this is a very "broad stroke" description of State law limitations on what federal tax laws refers to as "private activity." There are numerous permitted exceptions. Always talk first with your Library District Attorney when such matters come up!

CHAPTER FOURTEEN

Federal Tax Law Issues—Special Tax Provisions for Certain Buyers of Debt

Bank Qualified Debt—Basic Rules

The law before the 1986 tax reform disallowed a deduction for interest on indebtedness incurred or continued by a taxpayer to purchase or carry obligations the interest on which is exempt from Federal income tax. This rule applied to both individual and corporate taxpayers. Banks, however, had been largely exempted from this general rule. The 1986 Code changed this by denying banks a deduction for that portion of the bank's interest expense which is allocable to tax-exempt obligations (regardless of date of issuance) acquired by them after August 7, 1986 for taxable years that began after December 31, 1986. (The prior law rule allowing an 80% deduction for banks was continued for bonds acquired on or before August 7, 1986.)

The 1986 Code did, however, provide an exception to this rule which continues presently. Under the exception, a bank can purchase up to $10,000,000 ($30,000,000 in 2010) of the obligations of any governmental issuer who does not expect to issue in excess of $10,000,000 ($30,000,000 in 2010) of obligations in the calendar year in which the "bank qualified" debt is to be issued. This exception does *not* apply to the first $10,000,000 ($30,000,000 in 2010) in obligations of municipalities which plan to issue more than $10,000,000 ($30,000,000 in 2010) in the calendar year. This exception is limited to "qualified obligations" acquired by a bank. A bank can acquire as many of such obligations as it wishes of different issuers without limitation. For this purpose, "qualified obligations" include any obligation which (1) is not a private activity bond (e.g. school district general obligations), and (2) is designated by the issuer.

Obviously, not more than $10,000,000 of such obligations ($30,000,000 in 2010) may be designated for these purposes by any issuer during any calendar year. Moreover, it must be reasonably anticipated that the issuer will not issue more than $10,000,000 ($30,000,000 in 2010) of tax-exempt obligations (other than private activity bonds) in any calendar year, including any issues of "subordinate" governmental entities that are controlled by or derive their authority from the issuer in question. For issuers that meet these criteria, this is a cost-free way to make their obligations more attractive to bank purchasers.

In order for issuers to maximize their benefits from this exception, appropriate language must be inserted in notices of sale for applicable notes or bonds so that bidders will be aware that the obligations qualify for this treatment. When informal bids for notes are solicited orally, prospective purchasers should be similarly informed. Additionally, for qualifying issues that are sold without a printed notice of sale, Bond Counsel must be so informed so that the necessary insertions can be made in the certificate authorizing the issuance of such obligations, and a copy of such certificate must be provided to the purchaser.

How can a Library District determine if its Affiliated Entity will be an issuer that can issue bank qualified debt in a particular calendar year? Here are the steps:

Step No. 1: Does the Affiliated Entity reasonably expect to issue $10,000,000 ($30,000,00 for calendar year 2010) or less in tax-exempt bonds and notes in the calendar year? (small issuer question)

WHAT COUNTS:

1. All new money governmental general obligation issues (including those issued for the benefit of the Library District).
2. Advance Refundings (renewal more than 90 days in advance).
3. All governmental general obligation new money or advance refunding bonds or notes issued by a governmental entity subordinate to the municipality or issuing "on behalf of" same (i.e. certain I.D.A. debt may count).
4. All tax-exempt installment sales/ lease purchase agreements.

WHAT DOESN'T:

1. Private activity bonds or notes.
2. Current renewals (to the extent that the amount of the renewal does not exceed outstanding principal amount of maturing debt).
3. Most federally taxable debt obligations.

Step No. 2: Is the issue itself eligible for designated and qualified status? (issue qualification question)

A. New Money Issues—

1. Not a private activity bond or note (other than a 501(c)(3) obligation).
2. Not a taxable bond or note.

B. Renewal/Refunding Issues (Current or Advance)

1. Aggregate face amount does not exceed $10,000,000 / $30,000,000 (2010).
2. Each refunded bond or renewed note was part of an issue which itself did *not* qualify at the time for the $10,000,000 / $30,000,000 (2010) exception in its year of issuance and was *not* designated. (An issue renewing or refunding a designated bond or note will be deemed designated—see below.)
3. Not a private activity bond or note (other than a 501(c)(3) obligations.)
4. Not a taxable bond or note.

C. Certain Refundings/Renewals Or Designated Obligations May Be "Deemed Designated"

1. If a qualified and designated obligation is refunded/renewed, the refunding bonds or renewal notes are "deemed designated" if:

   a. The refunded/renewed obligation was both eligible to be designated and was actually designated.

   b. The par amount of refunding obligations does not exceed the outstanding amount of the refunded or renewal obligation. (Any excess can be designated.)

   c. The average maturity date of the refunding/renewal obligation is not later than the average maturity date of the obligations being refunded/renewed. Note: This rule by itself would eliminate renewal notes or bonds from qualifying when refunding/renewing typical 1 year notes so there is an exception:

   If the average maturity of the refunded debt is three (3) years or less, the requirement is waived.

   d. No refunding bond has a maturity date that is later than the date which is 30 years after the date that the original note or bond was issued.
2. Deemed designated obligations provide financial institutions with same benefit as designated obligations.
3. Deemed designated obligations do not count toward the $10,000,000/$30,000,000 limit of obligations which may be designated in a calendar year.

   Therefore more than $10,000,000 ($30,000,000 in 2010) may ultimately be issued, of which $10,000,000 / $30,000,000 is designated and the rest is renewals/refundings which are deemed designated.

D. Certain Obligations May Not Be Designated Or Deemed Designated:

1. Any refunding/renewal obligation when the aggregate face amount of the issue exceeds $10,000,000 / $30,000,000.
2. Private activity notes or bonds (other than 501(c)(3) obligations).
3. Taxable obligations.

Alternative Minimum Tax

The 1986 Code imposed an alternative minimum tax on individuals and a similar tax on corporations. Although the alternative minimum-tax on individuals existed before the new tax law, it was included from 1986 until 2009 in the computation of income interest on newly-issued private activity bonds (other than qualified 501(c)(3) bonds). In addition, corporations have had to treat 50% of the interest on *all* types of municipal obligations, including school district general obligations, as a preference item, regardless of when such bonds were issued. (That is, 50% of interest received on any tax-exempt obligations, including governmental activity general obligations, became subject to the corporate minimum tax.) In addition, interest income received by corporations was for some time includable in a corporation's tax base for purposes of computation of such corporation's liability for an additional 0.12% environmental corporate tax imposed by the "Superfund Amendments and Reauthorization Act of 1986" and later phased out.

Under a provision of the American Recovery and Reinvestment Act of 2009 (the "Recovery Act") interest earned on any new money bonds or notes issued in 2009 and 2010 and any bonds or notes issued in 2009 and 2010 to refund/refinance bonds or notes issued in calendar years 2004 through and including 2008 are not subject to the alternative minimum tax in any form.

New "Cost to Carry" Deduction for Banks in 2009 and 2010

The Recovery Act has also provided an additional incentive for bankers to buy the type of debt issued by an Affiliated Entity in 2009 and 2010 as it permits banks to avoid limits on interest expense deductions for new money, non-bank qualified bonds issued in 2009 and 2010 provided such bonds do not exceed 2% of its total assets

Under prior law, individuals and corporations are generally prohibited from deducting interest expense that they incur in order to acquire or carry tax-exempt bonds. However, as a matter of administrative policy, the IRS does not apply this rule to individuals and corporations (other than banks) whose holdings include only an insubstantial amount of tax-exempt bonds. Corporations generally meet this "insubstantiality" test if tax-exempt bonds comprise no more than 2% of their investment in active business assets; for individuals, tax-exempt bonds must comprise no more than 2% of their total investment portfolio and business assets.

Banks that hold tax-exempt bonds have not benefited from the IRS policy described above, and are generally prohibited from deducting a portion of their total interest expense. The non deductible portion is calculated based on the ratio of the bank's investment in tax-exempt bonds to its total investment in all assets. Bank Qualified Bonds are generally not counted as tax-exempt bonds for purposes of the investment ratio calculation.

To stimulate the purchase of tax-exempt bonds by banks, the Recovery Act allows banks to avoid any limitations on interest expense deductions for a limited amount of new-money, non-bank qualified bonds issued in 2009 and 2010. Thus, any new-money bonds issued in those years (whether or not they are private activity bonds) can qualify for exclusion from the investment ratio calculation. Each bank may only exclude 2009 and 2010 bonds up to 2% of its total investment in all assets; amounts beyond that limitation will be counted as invested in tax-exempt bonds in the investment ratio calculation and reduce the bank's deductible portion. Refunding bonds issued in 2009 and 2010 to refund bonds issued prior to 2009 will continue to be subject to the full interest expense deduction disallowance unless they are bank qualified bonds. However, refunding bonds issued to directly or indirectly refund 2009 and 2010 bonds that qualified for the exclusion will themselves qualify for the exclusion, regardless of when the refunding bonds are themselves issued.

CHAPTER FIFTEEN

Federal Disclosure Law Issues

The Official Statement ("OS")

Except in the case of direct lease financings with a vendor, leasing company or bank and financings where the securities are sold to a banker very limited number of sophisticated investors for investment rather than resale, the documentation in a debt financing includes a disclosure document, which is usually called an "official statement." The official statement is used to provide information to investors and prospective investors about the Affiliated Entity, the Library District and the bonds (or the free association library and the bonds in such cases). Bonds and notes constitute securities for purposes of state and federal securities laws and, therefore, the offering and sale of them through the official statement is subject to certain provisions of such laws, including, importantly, the antifraud laws. The official statement sets forth information about the terms of the securities, the security features, the sources and uses of the proceeds of the bonds, the issuer, any material risk factors in an investment in the securities, the documents under which the bonds or notes are issued and the tax-exemption of interest on the securities.

Prior to 1989, debt issuance by school districts and municipalities was not directly or indirectly subject to oversight by the U. S. Securities and Exchange Commission ("SEC"), except for general securities law rules governing the perpetration of "fraud on the market" by an issuer of debt found in the Securities Act of 1933 and the Securities Exchange Act of 1934, which have always applied to municipal securities.

Background of the Rule

In 1989, Rule 15c2-12 under the Securities Exchange Act of 1934 (the "Rule") was adopted to further protect investors in the municipal securities market from fraud and manipulation. Historically, the municipal securities market has been largely unregulated, but over the past twenty years the SEC has progressively introduced regulation designed to protect and inform investors.

The Rule requires an "underwriter," that is, one buying municipal bonds, notes, or other securities for purposes of resale in a primary offering, to obtain disclosure material or an "official statement," describing the issue and the issuer that is "deemed final" by the issuer. "Deemed final" means that the official statement is as complete and as accurate as possible, without (among other items, specifically referred to in the Rule) the principal amount(s), interest rate(s), offering price(s) and name of underwriter(s). Financial advisors work with issuers on their official statement for borrowing and bond counsel reviews it prior to distribution.

Before a competitive sale, "deemed final" official statements are provided to underwriters interested in bidding. After a competitive sale, the "deemed final" official statements which have been circulated to potential underwriters may then become final official statements by reprinting them, or attaching to them new covers or wrap-arounds with the final principal amount(s), interest rate(s), offering price(s), name(s) of underwriter(s), and other information which is reflective of the winning bid(s) (for example, if the issue is insured, the name of insurer, and information concerning the insurance). Final official statements must be printed in an adequate supply and provided to underwriters within seven days following the bond or note sale (or less, to permit underwriters to comply with applicable Municipal Securities Rulemaking Board ("MSRB") requirements, if delivery is scheduled for less than seven days of the sale).

In a negotiated sale, the underwriter must secure a contractual commitment, usually in the bond purchase agreement (the "BPA"), to be furnished with an appropriate quantity of final official statements within seven business days of the date of the BPA. MSRB Rule G-32 requires that one official statement and at least one official statement for each $100,000 of principal amount of the issue be furnished by the underwriter to each purchaser not later than the settlement date of their purchases. The official statement must be available to bond or note purchasers promptly after the date of sale, but no later than two business days before the date the securities are delivered to the underwriters.

Under the Rule, Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs") were proposed as a means to improve availability of official statements. Final official statements have been sent by underwriters to current NRMSIRs and kept on file. As of July 1, 2009 only one NRMSIR is now recognized by the SEC and it is operated by the MSRB and known as the Electronic Municipal Market Access System ("EMMA"). The role of the NRMSIRs (and hence, now EMMA) was increased under certain amendments to the rules further discussed below.

1994 Amendments

On November 10, 1994, the SEC adopted amendments (the "Amendments") to Rule 15c2-12 under the Securities Exchange Act of 1934, establishing disclosure requirements for municipal securities offerings in the secondary market. The Amendments, which are a modified version of those proposed by the SEC in a release dated March 9, 1994 (the "March Release"), were part of an ongoing process to improve the quality of information about municipal securities available to potential purchasers.

The SEC, among other things, regulates the underwriters that purchase municipal securities for resale. While, under current law, the SEC has limited power to regulate municipal issuers directly, the Rule, including the Amendments, has an impact on such issuers, because underwriters can purchase most municipal securities only after reviewing disclosure materials provided by the issuer. Furthermore, underwriters cannot recommend most municipal securities to their customers unless they have enough information to judge that the securities are an appropriate investment for their customers.

The Amendments require underwriters to determine that municipal issuers have agreed to provide ongoing disclosure to state and national repositories, including annual financial statements, operating data, and notices of "material" events that could affect such issuers' obligations, and that underwriters have systems in place to monitor such information concerning municipal bonds, notes and other securities being sold in the secondary market. Some municipal securities are exempt or partially exempt from the Amendments.

The Amendments have been effective since July 3, 1995.

The Amendments in Detail

The Rule was originally adopted to protect investors in the "primary" market (the market in which underwriters directly offer municipal bonds, notes or other securities purchased by them from issuers in either competitive or negotiated sales). The Amendments are intended to offer protection to investors in the "secondary" market (the market in which the securities are traded or resold). Although much of the general obligation notes offered by issuers in New York State are purchased directly by banks or other institutions and held in their portfolios and not reoffered (and those that are reoffered are often purchased for mutual funds by dealers), it is important to become familiar with the Amendments.

Secondary market disclosure is viewed by the SEC and others as necessary because purchasers of municipal securities in the secondary market should have access to current financial information and operating data in order to evaluate the securities they are interested in selling or purchasing in the secondary market. The current financial information and operating data presented in the final official statement that is prepared for the initial offering certainly will change over time, possibly affecting the value of the securities. The purpose of the Amendments is to make available, to purchasers in the secondary market, the most current financial and operating information regarding issuers. The SEC believes that accessible, periodic updates from issuers are a way to assure orderly markets and fairness to all participants.

Under the Amendments, underwriters will require as a condition of purchase that, among other things, issuers provide in the future reviewable information, in a timely fashion. The Amendments required underwriters have systems in place, by January 1, 1996, for reviewing such information. Generally, underwriters are now prohibited from purchasing or selling municipal bonds, notes and other securities (unless such securities fit within an exemption to the Rule as amended) unless they determine that the issuer (or obligor on the securities for conduit-type issues) has undertaken a written agreement or contract for the benefit of the holders of bonds, notes or other securities, to provide annual financial information and notices of material events (notices of material events are explained further below).

Under the Amendments, underwriters cannot agree to purchase bonds or notes in competitive or negotiated sales unless they have reasonably determined that the issuer has agreed in writing to provide ongoing disclosure of annual financial information and notices of material events (unless the issue is exempt under the Amendments, or partially exempt; see “Exemptions” herein).

The effective dates of the Amendments were designed to allow issuers, underwriters, and other market participants enough time to develop and implement the procedures necessary to comply therewith. The first step is a covenant by the issuer, for the benefit of holders of bonds, notes or other securities, to provide ongoing secondary market disclosure of annual financial information and notices of material events to the NRMSIRs and state information depositories (“SIDs”) or as of July 1, 2009 solely to the MSRB.

The official statement for the primary offering sets the standard for ongoing disclosure. Future financial information and operating data must be provided for those persons, entities, enterprises, funds and accounts that are necessary for an evaluation of the offering. The SEC suggested in an interpretive release dated November 10, 1994 (the “November Release”) that in the case of a general obligation offering, demographic statistics should be considered as operating data.

The official statement must contain a description of the agreement to provide ongoing financial information and operating data and notice of material events, as well as the scope of that ongoing disclosure. An Affiliated Entity will need a covenant from the Library District to assist it in this compliance for bonds issued on behalf of the Library.

At the time of the primary offering, the participants in an offering (for example, the issuer, the purchaser, and the insurer, if any) will decide what type of information is material to the offering and who is responsible for providing ongoing information to repositories. As stated above, the final official statement will set the standard for what type of information this will be. The final official statement would either contain financial information and operating data or refer to documents prepared and previously made publicly available, containing such information.

The participants in the primary offering will also commit to provide annual financial information for subsequent years by a particular date. The SEC originally proposed that issuers be required to produce annual audited financial statements, which was considered quite burdensome by many of those who commented on the proposed Amendments. As adopted, the Amendments do not require that all issuers produce audited financial statements. However, if an issuer or obligor does produce audited financial statements, they must be delivered to the NRMSIRs. The accounting principles used in preparing such statements must be stated, and financial information should be reasonably consistent to enable year to year comparisons. Annual financial information may reference other information already on file with the NRMSIRs and SIDs or the MSRB.

In addition to annual financial disclosure, the Amendments list eleven "material" events requiring notice to the secondary market, in a timely manner ("timely" has not been defined by the SEC, and could be interpreted to mean as soon as reasonably possible), by delivery to NRMSIRs or the MSRB and the appropriate SIDs until July 1, 2009 and as of this writing only to the MSRB:

- principal and interest payment delinquencies
- nonpayment related defaults
- unscheduled draws on debt service reserves reflecting financial difficulties
- unscheduled draws on credit enhancements reflecting financial difficulties
- substitution of credit or liquidity providers, or their failure to perform
- adverse tax opinions or events affecting tax-exempt status of the security
- modifications to rights of security holders
- bond calls
- refundings
- release, substitution, or sale of property securing repayment of securities
- rating changes

In addition, notice of any failure of the issuer (or other obligor) to provide annual financial information by the date specified in the written agreement generally must also be disclosed to repositories, which is discussed below. Any failure to comply with the written agreement to provide secondary market disclosure within the previous five years must be disclosed for bond issues. The SEC recommends, but does not require, that issuers file notice of favorable events, including cure of an adverse event listed above.

Underwriters must now have in place, systems designed to monitor material event disclosure, and must have "reasonable assurance" that they will receive prompt notice of material events before they can recommend purchase of a municipal security to their customers. Although this appears to be a limitation placed only on underwriters, this is also a concern for issuers as well, because if a dealer is unable to recommend or sell a security, they are unlikely to purchase it in either the primary or secondary market.

Annual financial information and notice of material events (the ones listed above) must be sent by issuers (or the obligors in conduit issues), to all NRMSIRs or the MSRB and the appropriate SID (in the state of issuance, if such depository exists) until July 1, 2009 and as of this writing only to the MSRB.

The SEC required that NRMSIRs be national in scope, maintain current accurate information, and have effective retrieval and dissemination systems. They cannot place limits on the persons from which they will accept information from, and must provide access to documents to anyone willing to pay the fees. They must charge "reasonable" fees, and may not charge issuers for filing information.

In the November Release, the SEC encouraged and offered guidance to states developing SIDs. As mentioned above, if an appropriate SID exists, notices of material events and annual financial information were to be submitted to such SID as well as the NRMSIRs or the MSRB. With the takeover of the NRMSIR function solely by the MSRB on July 1, 2009, SIDs, if any, will likely cease to operate.

The New York State Comptroller's Office already collects most debt statements, official statement filings, and reports of financial condition, as required under Section 30 of the New York State General Municipal Law. New York State never did establish an official SID.

Exemptions

The Rule fully exempts some issues. The Rule does not apply to issues with principal amounts under $1,000,000. The Rule also only applies to issues purchased from the issuer by an underwriter with a view to offer or sell. If the issue is being purchased privately for the portfolio of an institution, for example, a bank buying a bond anticipation note that such bank will hold in its own portfolio, the Rule does not apply (regardless of the principal amount).

An issue of bonds, notes or other municipal securities, which is otherwise subject to the Rule, that is sold in denominations of $100,000 or more is not subject to the Rule, if such issue: i) is sold to no more than thirty-five (35) "sophisticated" investors (investors who are believed to have the knowledge and experience in financial matters to evaluate the merits and risks of such issue) who are not purchasing for distribution; or ii) has a maturity of nine months or less, or has a put option exercisable at least every nine months (a put option is the opportunity for the owner to request that the issuer, directly or through an agent, redeem or purchase such security at par value or more).

The Amendments provide limited exemption for securities with maturities of eighteen months or less. Annual financial and operating information are not required for these securities, but issuers are still required to agree to provide notices of material events to the NRMSIRs or the MSRB and appropriate SIDs, until July, 2009, and thereafter, to the MSRB.

Issuers with less than an aggregate of $10,000,000 in outstanding debt (including the obligations offered and excluding securities that were offered in transactions exempt under the Amendments), were exempt from the annual financial information requirement of the Amendments if such issuers made a "limited undertaking" (the term used in the Amendments) to provide financial information and operating data on request (they must also specify what type of information that is), or provide such information annually to an SID. An agreement to provide the financial and operating data that is generally prepared and available to the public satisfied such limited undertaking. Issuers using this exemption had to describe in the final official statement where the financial information and operating data would be obtained and from whom. However, recent revisions to this provision have effectively eliminated this special undertaking, and now practically speaking such smaller issuers have the same responsibilities as those with $10,000,000 and over in outstanding debt.

Compliance

Frequent issuers, and those with full time finance staffs have been able to meet the new requirements with the least difficulty. However, disclosure in official statements needs constant updating and revision. Issuers must covenant to provide ongoing information (unless, of course, the issue is exempt). Nowadays, appropriate modifications to customary bond and note proceedings accommodates the inclusion of such covenants.

It is important for issuers to understand the implications of Rule 15c2-12 because failure to comply may have several potential repercussions. At the very least, failure to provide ongoing information will cause the market to react unfavorably the next time such an issuer tries to sell its bonds or notes. A refusal to make a covenant would severely limit the market of an issue.

While your bond counsel will certainly want to review your compliance with the Rule and its Amendments, including any Official Statement prepared by a financial advisor with the help of an Affiliated Entity in connection with a public offering of debt, it is ultimately the responsibility (and liability) of the issuer to ensure that the Official Statement or other disclosure compliance document is 100% accurate. The standard to which the Affiliated Entity will be held is as follows:

> "The statements contained in the Final Official Statement dated __________, 200_ do not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading."

There is a limited exception for data from other sources.

That is the general antifraud requirement of the securities law applicable to any municipal securities offering in the public markets of any school district or municipality in the State.

Responsibilities and Liabilities

As noted above, the antifraud provisions of the 1933 Securities Act and the 1934 Securities Exchange Act require that the information provided in connection with the offer or sale of securities must not contain any untrue statement of a material fact and must not omit to state a material fact necessary to make such information not misleading. This is of critical importance. The issuer is primarily liable for any material misstatements or omissions regarding the issuer made in the documents used to offer and sell the securities. The issuer may not transfer this primary liability to its underwriter, its financial advisor, district counsel, bond counsel or any of the other parties involved in the financing. Such parties might be liable in their own right, but their liability will not absolve the issuer of its primary liability. Consequently, the issuer and its staff must make every effort to ensure that the issuer's offering documents are accurate and complete. The SEC has stated that:

> "Because they are ultimately responsible for the content of their disclosure, issuers [of municipal securities] should insist that any professionals retained to assist in the

> preparation of their disclosure documents have a professional understanding of the disclosure requirements under the federal securities laws."

In connection with its Orange County, California bankruptcy investigations, the SEC reiterated that issuers "bear the most significant responsibility to ensure" disclosure is adequate, and commented that:

> "[A] public official may not authorize disclosure that the official knows to be false; nor may a public official authorize disclosure while recklessly disregarding facts that indicate that there is a risk that the disclosure may be misleading."

In short, always read the draft official statement generated to sell debt on your behalf. You will not be responsible for the information about the Affiliated Entity, but you will be responsible for the information disclosed therein about the Library District.

CHAPTER SIXTEEN

Post-Issuance Responsibilities, Issues and Problems

After issuance of any cashflow or capital debt obligation, there are several areas of continuing responsibility for the issuer (besides paying back the bond or note holders for the loan of their money—highly recommended) as well as certain typical problem scenarios.

The areas of responsibility include proper investment of borrowed proceeds within LFL, General Municipal Law and Federal tax law guidelines, compliance with the federal reporting, arbitrage and arbitrage rebate rules, compliance with ongoing federal disclosure requirements, and proper reporting to State oversight authorities.

There are also some fairly typical problem scenarios which may arise, such as: (a) not enough money to finish a project; (b) too much money authorized, or authorized and borrowed for a project; and (c) issues surrounding reimbursement of moneys temporarily borrowed on an inter-fund basis to be repaid with debt proceeds upon issuance.

Responsibility: Investment of Borrowed Proceeds

The proceeds received upon the sale and issuance of debt obligations must, in most cases, be treated differently from other moneys raised by the tax levy or from other sources. While TAN, RAN or budget note proceeds may be treated like general fund moneys, moneys received from the sale of BANs or bonds to finance the cost of capital projects must be kept and accounted for separately.

The proceeds, inclusive of premiums, from the sale of bonds, bond anticipation notes, capital notes, urban renewal notes (a form of note similar to a specialized RAN) or budget notes must be deposited and secured in a special account in the manner provided by Section 10 of the General Municipal Law. Such capital proceeds cannot be commingled with other funds of the issuer, and must be expended only for the object or purpose for which such obligations were issued. Capital fund moneys cannot be utilized for inter-fund loans. In the event that any portion of the proceeds, inclusive of premiums, from the sale of bonds, bond anticipation notes, capital notes, urban renewal notes or budget notes is not expended for the object or purpose for which such obligations were issued, such portion must be applied only to the payment of the principal of and interest on such obligations, respectively. Notwithstanding the foregoing provisions of the LFL, the Board of Trustees of any Library District may adopt any or all of the following resolutions to provide that:

a. The proceeds, inclusive of premiums, of capital notes issued in amounts of $100,000 or less, and of budget notes, need not be deposited in a special account but may be deposited and commingled with other funds of the issuer in any account of the issuer in a bank or trust company located and authorized to do business in the State, but such power should not be construed as authorizing the use of such proceeds for an object or purpose other than that for which the obligations were issued.
b. The proceeds, inclusive of premiums, from the sale of any two or more issues of bonds, bond anticipation notes, capital notes, urban renewal notes or budget notes need not be deposited in separate special accounts but may be deposited in a single special account of the issuer in a bank or trust company located and authorized to do business in the State, but should not be commingled with other funds of the issuer. The chief fiscal officer should then maintain a separate accounting record of each issue to ensure that the proceeds shall be used only for the object or purpose for which the obligation was issued.
c. Moneys appropriated for a purpose for which bonds, bond anticipation notes, capital notes or urban renewal notes have been authorized may be deposited in the same bank account with the proceeds from the sale of such obligations. Such power should not be construed as authorizing the use of the proceeds of such obligations for an object or purpose other than that for which they were issued. Any moneys remaining in such bank account after the object or purpose has been completed or abandoned must be applied to the payment of the principal of and interest on such obligations. Any excess remaining thereafter may be used for any lawful purpose.

The proceeds, inclusive of premiums, from the sale of bonds, bond anticipation notes, capital notes and urban renewal notes are to be invested in the manner provided by Section 11 of the General Municipal Law which provides a list of permitted investments. Such investment is to be made by the Board or more typically the chief fiscal officer, if the Board, as is customary, shall delegate such duty to that person. The separate identity of the proceeds from the sale of bonds, bond anticipation notes, capital notes, urban renewal notes and budget notes is to be maintained at all times, whether such proceeds consist of cash or investments or both. Any interest earned or capital gain realized on any investment is to be applied to either the payment of the principal of and interest on the bonds, bond anticipation notes, capital notes, urban renewal notes or budget notes, as the case may be, the proceeds from the sale of which were used in making such investment or for any other purpose or purposes for which such issue of bonds, capital notes or urban renewal notes has been authorized. However, any interest earned or capital gain realized on any investment, to the extent necessary to maintain the exemption from federal income taxation of interest on the obligations the proceeds from the sale of which were used in making such investment, is to be paid to the United State Treasury Department.

Where the proceeds from the sale of bond anticipation notes have been invested and such notes have been retired from the proceeds from the sale of the bonds in anticipation of which they were issued, any interest earned or capital gain realized on any investment is to be applied only to the payment of the principal of and interest on the bonds.

Investment of such moneys are regulated by the provisions of Sections 10 and 11 of the General Municipal Law, and the possible application of the yield restriction rules of the U.S. Treasury regulations promulgated under Section 148 of the Internal Revenue Code of 1986, as amended (the "Code"), previously discussed.

Responsibility: Compliance with Federal Reporting, Arbitrage and Arbitrage Rebate Regulations

Because the interest on general obligation bonds and notes issued by school districts and municipalities in the State is generally tax-exempt to the holders thereof for federal income tax purposes under Section 103 of the Code, each issuance of such debt is subject to the federal requirement that a Form 8038-G or Form 8038-GC be filed within regulatory deadlines. Bond counsel assists in completion of these forms. These are "information returns" by which the Internal Revenue Service is able to track all tax-exempt municipal debt issuances in the United States. Random audits of governmental debt has become more commonplace in the new millennium.

It is also part of the job of bond counsel to inform any issuer and their local counsel of the applicability of the federal arbitrage rules governing the period of time, if any, during which borrowed proceeds may be invested without restriction as to yield and the arbitrage rebate rules (and exceptions) governing the provision to the U. S. Treasury of certain investment earnings on borrowed proceeds, accrued prior to expenditure on the purpose for which the debt was borrowed. *See* Chapter 12 herein. The issuer may need a rebate compliance provider to help with annual calculations. The Library District will need to assist in this process. It is not optional.

Responsibility: Compliance with Federal Disclosure Rules

Any governmental debt issuance in the public markets, national, state or local, is potentially subject to the effect of Rule 15c2-12 of the U.S. Securities and Exchange Commission ("SEC") promulgated under the Securities Exchange Act of 1934, as amended. While the SEC does not directly regulate municipal or school district issuers, it does regulate the bond markets and it does have authority to take legal action against municipal or school district issuers in connection with fraud or misrepresentations in the sale of their debt. It is again part of the role of bond counsel to advise issuers and their local counsel as to any Rule 15c2-12 disclosure requirements upon the sale of debt, and ongoing thereafter to maturity. The Rule does fully exempt some issues and certain small issuers are subject to less onerous reporting requirements.

However, any debt issuance of over $1,000,000 nowadays will usually involve production of an "official statement." The production of an official statement is a joint work product of an issuer and its financial advisor, local counsel and bond counsel. This is the municipal equivalent of a corporate prospectus plus annual report. The official statement is a general overview of the current financial and related circumstances of the issuer and its tax base. The standard for the inclusion of information in an official statement is straight forward: it must be the case that the statements contained in the Official Statement do not contain any untrue statements of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading.

In order to sell such debt, an issuer will need to contract to update certain of the information in the official statement for the life of an issue. Which information needs updating and when are a function of the type of debt and the size of the issuer. Bond counsel must be familiar with these rules and advise local counsel and the issuer and its financial advisor accordingly. See Chapter fourteen herein.

Responsibility: State Oversight Reporting

The issuance of serial bonds must be reported to the Office of the State Comptroller both in the annual report thereto as well as the filing of a debt statement, prior to the public sale of any issue of serial bonds.

Not more than fifteen nor less than three days before any school district or municipality having an aggregate assessed valuation of taxable real property of $100,000 or more, sells any bonds which are required to be sold at public sale, it must file with the State Comptroller a verified statement of its debt-contracting power prepared as of the date not more than thirty days previous of the date of the sale of such bonds. The statement is to show the amount of obligations proposed to be sold at such sale. A duplicate copy of every such debt statement is to be filed in the same respective period of time with the clerk of such School District.

Such statements are to be prepared in the manner prescribed in title ten of article 2 of the LFL. Any error, defect, omission or inaccuracy in any such statement, or in the manner of its execution or filing, will not affect the validity of any obligations.

Therefore the annual report must include the latest debt information.

Post-Issuance Issues: Insufficient Funds

Turning now to some typical post-issuance problem areas, insufficient borrowed proceeds to finish a project is not an uncommon scenario.

Investment earnings which have been made on the borrowed proceeds prior to their expenditure, must be used to pay arbitrage rebate to the federal government, if applicable, or debt service on the debt obligations and is generally (but not exclusively) not available for project costs in the general obligation context. In any event, even if available for the capital purpose, it would be necessary for your voters to authorize the capital project first at the increased cost.

Assuming insufficient available funds from any other source, the only option is for the Board of Trustees to call for a new election authorizing the issuance of additional debt for the capital project. This would be subject to precisely the same pre-adoption proceedings referendum requirements as the initial bond resolution.

Post-Issuance Issues: Too Much Money Authorized

Everyone should have this problem: the Board of Trustees has authorized a higher maximum estimated cost and debt issuance than the project as originally envisioned requires. What to do? It is first useful to note what cannot be done:

a. the excess authorized amount cannot be used on some other capital project.
b. the excess authorized amount cannot be used for any general fund or other fund operating purposes.

If the excess has already been borrowed at the time it is determined to be excess, it must be used to pay debt service on the obligation from whence it is proceeds at the next available debt service payment date(s). It is only when no such debt service remains, that such excess proceeds may be used for any lawful purpose, subject to federal yield restriction, arbitrage and arbitrage rebate rules.

Excess authorization which is not utilized or otherwise encumbered may be repealed, or, pursuant to Section 41.00 of the LFL, will automatically self-repeal ten years after the date of adoption.

Post-Issuance Issues: Reimbursement Issues

Often, prior to authorizing the financing of a capital project, a Library District may expend available funds in connection with some initial or preliminary costs relating to the project. It is generally understood by all concerned that, if and when the project moves ahead, those available funds will be reimbursed from the proceeds of a borrowing, hopefully within the same fiscal year. (A Library District should never sign contracts for capital projects work which will be bond-financed (other than preliminary planning costs) prior to the referendum and adoption of the implementing bond resolutions of the Affiliated Entity.)

Both the LFL and the U.S. Treasury Regulations promulgated under Section 148 of the Code have specific rules regarding the reimbursement of previously expended available funds.

Section 165.10 of the LFL provides that if there are funds other than the proceeds of bonds, bond anticipation notes, capital notes and budget notes, and funds which, by law, may be used only for stated purposes, which are not immediately required for the purpose or purposes for which the same were borrowed, raised or otherwise created, the Board of Trustees may authorize the temporary use of such funds for the purpose or purposes for which an issue of bonds or capital notes has been authorized. Suitable records must be kept of the temporary diversion of such funds. Such funds are to be made again available to the Library District from the proceeds of such bonds or capital notes or from the proceeds of the sale of bond anticipation notes issued in anticipation of the sale of such bonds.

Therefore, if a valid bond resolution is not in place (including any applicable referendum having successfully occurred), at the time available moneys are advanced, they may not be reimbursed from later borrowing proceeds. Nevertheless, this practice continues to occur with some regularity. It can be the subject of criticism on audit by the Office of the State Comptroller. It is preferable to simply adopt a bond resolution prior to the temporary advance, without borrowing the funds in the public markets, and thus without starting the PPU clock running, but this is not possible for Library District preliminary project expenses incurred prior to the referendum.

The adoption and public approval of a bond resolution by the Affiliated Entity will also cover the Library District with regard to the federal bond reimbursement regulations. These regulations generally require a "statement of official intent" prior to temporary advances of available moneys. A properly drafted bond resolution may serve as an official notice of intent to borrow under these Treasury Regulations as well as LFL Section 165.10. *In addition, a Library Board of Trustees should itself state its intent to reimburse at the earliest possible date when planning for any capital project.*

Post-Issuance Issues: Change in Capital Project Elements

The Library District has a voter approved proposition, it has an approved bond resolution, it is proceeding with its building plans and financing plans, and then something happens: some element costs a lot more than anticipated due to price increases or scarcity, a corporation that had planned a major expansion at a local facility with a significant influx of new families goes bankrupt and the new branch is really not needed, some element needs revision due to a previously unconsidered aspect. What to do? What are the rules?

Boy, you ask difficult questions. This is a tough one and a lot depends on the specific facts and circumstances. Therefore, it is only possible here to set out some of the key considerations:

1. People who voted for your capital program may have done so in anticipation of a particular element that now is under reconsideration or revision from that presented to the public before the vote. But for inclusion of that major element, they might have voted "no."
2. The Board of Trustees does have discretion within the voter mandate and it has a fiduciary obligation to not waste assets of the Library District. This is a representative form of government, not direct micromanagement by the public.
3. If the proposition used the broad language of a class of objects or purposes, the voters could have rejected it and called for the proposition language to be more specific.
4. What language did the Library District information materials use? Was some element presented as definite?

5. A health, safety or welfare concern which leads to a change is a strong reason for revision.
6. A Board of Trustees can order a special election to reallocate portions of a previously authorized project if the moneys have not yet been borrowed.
7. Proposition language which includes words like “incidental improvements,” “ancillary work” or “related improvements” is intended to cover unexpected change orders and “while we are in there” type work. The word “including” does not mean the list following it is everything else.
8. An approved proposition can be rescinded only by a public vote of the qualified voters. Some cases hold that the affirmative vote is a mandate, unless and until so rescinded, especially if others have since relied on the vote in some way.
9. The maximum estimated cost of the project(s) presented to the voters cannot, in any event, be exceeded for work on said project(s) as described in the proposition, regardless of the source of additional moneys, without a further vote of the people.
10. Proceeds from Bonds or BANs authorized for an object or purpose may never be utilized for a different object or purpose. Never. Not Ever. Just No.

CHAPTER SEVENTEEN

Lease Purchase Agreements, Energy Performance Contracts and Certificates of Participation

General Municipal Law Section 109-b. An "installment purchase contract" means any lease purchase agreement, installment sales agreement or other similar agreement providing for periodic payments between a corporation, person or other entity and a political subdivision which has as its purpose the financing of equipment, machinery or apparatus under General Municipal Law Section 109-b. General Municipal Law Section 109-b authorizes political subdivisions to enter into installment purchase contracts (also known as lease purchase agreements) to finance certain capital equipment and to cause or permit certificates of participation to be issued in connection therewith. Bond counsel participation in these transactions is customary to ensure validity and the tax-exempt status. "Political subdivision" is defined to include "a municipal corporation, school district corporation or board of cooperative educational services." A "municipal corporation" is defined in Section 66 of the General Construction Law to include a county, city, town, village and school district while a "district corporation" must have the power to contract indebtedness *and* to levy taxes or benefit assessments. Libraries would seem to fit solely within the definition of an "education corporation" or a "not-for-profit corporation" in said Section 66 or "education corporation" in Section 216 -a of the Education Law, and not within these other definitions.

Is General Municipal Law Section 109-b applicable to Library Districts? Apparently not, unless by the indirect route of the authority found in Section 216-a and 226 of the Education Law. Does that mean a library cannot enter into an installment purchase contract? No. Such authority may well reside in the general powers of an "education corporation" or a not-for-profit corporation, and although General Municipal Law Section 109-b may not apply, you may want to know the rules that the State generally thinks are important in this area of financing. If so, read on.

A political subdivision may enter into an installment purchase contract subject to the following restrictions:

a. The governing board of a political subdivision must adopt a resolution authorizing the installment purchase contract, much like a bond resolution.

(1) If an authorization for the issuance of the obligations to finance the equipment,

machinery or apparatus would have been required by law to be subject to a permissive or mandatory referendum, then the authorization to enter into an installment purchase contract is subject to a permissive or mandatory referendum, as the case may be, in the same manner as provided for such referendum on the issuance of obligations.

(2) If the authorization for the issuance of obligations to finance the equipment, machinery or apparatus would have been required by law to be subject to: (i) a certain supermajority vote of the governing board, (ii) a mandatory or permissive referendum, or (iii) both, then the authorization to enter into an installment purchase contract for equipment, machinery or apparatus is subject to such vote, referendum or such referendum and vote, as the case may be, in the same manner as provided for such vote and/or referendum on the issuance of obligations.

(3) If the authorization for the issuance of obligations would have been subject to a referendum only if the obligations had a maturity of more than five years or not less than some other minimum period, then the authorization to enter into the installment purchase contract is subject to referendum only if the term of the contract is equal to or more than such minimum period of maturity.

b. The term of such installment purchase contract, including all renewals thereof, cannot exceed the period of probable usefulness prescribed by section 11.00 of the Local Finance Law for equipment, machinery or apparatus being financed under the installment purchase contract.

c. The installment purchase contract must separately state the principal and interest component of the periodic payments to be made thereunder. The total of all periodic payments which include both principal and interest components made by the political subdivision during each year throughout the term of the installment purchase contract must be substantially level or declining.

d. An installment purchase contract must contain the following clause: "This contract shall be deemed executory only to the extent of moneys appropriated and available for the purpose of the contract, and no liability on account thereof shall be incurred by the political subdivision beyond the amount of such moneys. The installment purchase contract is not a general obligation of (insert name of political subdivision(s)). Neither the full faith and credit nor the taxing power of (insert name of political subdivision(s)) are pledged to the payment of any amount due or to become due under such installment purchase contract. It is understood that neither this contract nor any representation by any public employee or officer creates any legal or moral obligation to appropriate or make moneys available for the purpose of the contract."

e. No payment under the installment purchase contract except payment for the total amount outstanding can be financed from the proceeds of obligations issued pursuant to the Local Finance Law other than the proceeds of revenue anticipation notes, tax anticipation notes or budget notes due to cashflow needs. An installment purchase contract may thus be paid off in full with the issuance of duly authorized BANs or serial bonds.

f. There are additional provisions if an installment purchase agreement is to be made a part of a certificate of participation instrument for wider sale of the financing contract to the general public.

g. Installment purchase contracts for equipment, machinery or apparatus do constitute purchase contracts for public bidding purposes and are subject to public bidding requirements to the extent applicable by law. For purposes of determining whether the cost of the equipment, machinery or apparatus exceeds the monetary threshold fixed in section one hundred three of the General Municipal Law relating to competitive bidding, the cost of the equipment, machinery or apparatus, exclusive of the cost of financing is considered. If the equipment, machinery or apparatus is to be financed by a party other than the party submitting the bid, the bid specifications may provide that the political subdivision may assign its right to purchase to a third party without the necessity of approval by the other party to the contract. Nothing precludes a school district from advertising for bids in the alternative with and without financing.

h. Each political subdivision shall have the power to enter into agreements providing credit enhancement with respect to the installment purchase contract, but any reimbursement obligation of the political subdivision is subject to appropriation by the legislative board.

It is important to note installment purchase contracts made pursuant to this section of law, do *not* constitute or create indebtedness of the state or the political subdivision for purposes of article seven or eight of the state constitution or section 20.00 of the Local Finance Law, nor do they constitute a contractual obligation in excess of the amounts appropriated therefore. Neither the state nor a political subdivision has any continuing legal or moral obligation to appropriate money for said payments or other obligations due under the installment purchase contract. No installment purchase contract is permitted to contain any provision which, in the event of non-appropriation, precludes a political subdivision from acquiring equipment, machinery or apparatus for the same or similar purpose as the equipment, machinery or apparatus included in the installment purchase contract for a period of more than sixty days from the date of expiration, termination or cancellation of such contract, provided, however, that in no case can an installment purchase contract contain any provision which would preclude a political subdivision from performing any statutorily or constitutionally required duties or functions, or require the political subdivision to pay liquidated damages.

In the case of the failure to appropriate, the sole security, apart from any security provided by a credit enhancement, for any remaining periodic payments is the equipment, machinery or apparatus subject to the installment purchase contract. Any installment purchase contract may provide that the installment purchase contract is secured by the underlying equipment, machinery or apparatus and that, in the event the political subdivision fails to appropriate funds sufficient for payments required under the contract, the financed equipment, machinery or apparatus may be sold on behalf of the persons entitled to receive payments under the installment purchase contract, provided that any excess proceeds from such a sale, after deduction for and payment of fees, expenses and any taxes levied on sale, plus accrued interest must be paid to the political subdivision.

What a rating agency may think of a failure to appropriate is another matter entirely.

The aggregate amount of unpaid periodic payments, excluding interest, to be made under any outstanding installment purchase contract is to be deemed to be existing indebtedness solely for the purpose of determining the power of any political subdivision to contract indebtedness under the debt limitations of section 104.00 of the Local Finance Law. No political subdivision can enter into any installment purchase contract if the amount of unpaid periodic payments, excluding interest, proposed to be made under such installment purchase contract and those outstanding, together with the amount of outstanding indebtedness, would exceed one hundred fifty percent of the limit prescribed by such section 104.00 or if the total amount of such payments, excluding interest, under such proposed contract and those outstanding would exceed forty percent of such limit.

A political subdivision does not have the power to enter into an installment purchase contract except as authorized in Section 109-b of the general municipal law and general municipal law Section 109-b does not authorize the conveyance or lease of property owned by a political subdivision except as otherwise authorized by law.

All installment purchase contracts of a school district or municipality and the interest thereon, are exempt from taxation for municipal and state purposes.

The State Comptroller's Rules

Subparagraph (d) of subdivision (3) of General Municipal Law Section 109-b requires the State Comptroller to adopt rules "governing the procedure which shall be adhered to when entering into installment purchase contracts or authorizing the execution and delivery of certificates of participation. . . ." The primary purposes of these rules are to:

a. cause a political subdivision to evaluate critically the financing alternatives available to it under Section 109-b of the General Municipal Law and the LFL;
b. ensure that a political subdivision, when procuring the capital improvements to be finances, complies with the competitive bidding requirements of article 5-a of the General Municipal Law or any other general, special or local law or, if such competitive bidding requirements are not applicable, the policies required to be adopted pursuant to General Municipal Law, Section 104-b; and

c. require a political subdivision to seek competition for financing unless the political subdivision determines that it is in its best interest to conduct a private sale of certificates of participation.

Definitions. For purposes of the State Comptroller's regulations governing installment purchase contracts, the following definitions apply.

a. *Cost of financing* shall mean the total payments of principal and interest estimated to become payable pursuant to an installment purchase contract or due on indebtedness, as the case may be, together with any estimated actual and necessary expenses incurred in connection with the execution of such installment purchase contract or the issuance of such indebtedness to the extent such expenses are not included in the periodic payments to be made under the installment purchase contract or aid from the proceeds of the indebtedness.
b. *Evaluation of financing alternatives* shall mean the evaluation prepared pursuant to the criteria indicated below.
c. *Indebtedness* shall mean bonds or notes issued in accordance with the LFL.
d. *Political subdivision, capital improvement, installment purchase contract* and *certificate of participation* shall have the meaning ascribed to them by paragraphs (a) through (d) inclusive of subdivision (1) of Section 109-b of the General Municipal Law.
e. *Pooled* or *aggregate program* shall mean any program under which certificates of participation are issued and represent a proportionate interest or the right to receive a proportionate share in lease, rental, installment or other periodic payments made or to be made by a political subdivision and one or more parties, other than the political subdivision, pursuant to installment purchase contracts.
f. *Private sale* shall mean any sale of certificates of participation, other than a public sale, conducted by a political subdivision.
g. *Public sale* shall mean any sale of certificates of participation conducted by a political subdivision pursuant to the regulations.

The following rules of the State Comptroller are currently in effect:

Evaluation of financing alternatives. No Board is permitted to adopt a resolution authorizing an installment purchase contract unless an evaluation of financing alternatives has been prepared in connection therewith. Such evaluation shall set forth the financing alternatives considered and the criteria used to evaluate these alternatives. The evaluation must also contain written documentation substantiating the estimates required to be included in the evaluation pursuant to this section. At a minimum, the evaluation of financing alternatives must contain the following:

a. a statement indicating the estimated cost of each capital improvement to be financed, exclusive of the cost of financing;

b. a statement indicating whether the proposed capital improvements may be financed with indebtedness issued under the LFL and if not, the specific reasons why such financing is not authorized;
c. if the capital improvements may be financed with indebtedness, a statement indicating the estimated total cost of the capital improvements, inclusive of the cost of financing, if financed pursuant to the LFL;
d. a statement indicating the estimated total cost of the proposed capital improvements, inclusive of the cost of financing, if financed pursuant to an installment purchase contract;
e. a comparison of the estimated total costs required by subdivisions (c) and (d) of this section; and
f. a recommendation as to whether it is in the best interests of the political subdivision to finance the capital improvements pursuant to the LFL or pursuant to an installment purchase contract and the specific reasons for such recommendation.

Adoption of resolution authorizing an installment purchase contract. Any resolution authorizing a political subdivision to utilize an installment purchase contract to finance capital improvements must refer to the evaluation of financing alternatives and, after taking into account such evaluation, set forth the specific reasons why the governing board has determined that it is in the best interests of the political subdivision to finance the capital improvements pursuant to an installment purchase contract. The evaluation of financing alternatives must be maintained as a public record and be filed with the resolution to which it pertains.

The resolution to be adopted is subject to the same rules of adoption as those governing bond resolutions.

Compliance with competitive bidding statutes or other applicable provisions. No political subdivision can enter into an installment purchase contract unless and until it has complied with the competitive bidding requirements of article 5-A of the General Municipal Law or of any other general, special or local law. If no such competitive bidding requirements are applicable, the political subdivision must comply with its own procurement policies and procedures adopted pursuant to General Municipal Law, Section 104-b. For purposes of complying with such requirements or procedures, a political subdivision may determine to solicit bids, quotations or proposals, as the case may be, in the alternative, exclusive and inclusive, of the cost of financing.

Procurement of vendor and non-vendor financing. If the Board determines that it is in the best interest of the school district or municipality to select a bid, offer or proposal, as the case may be, inclusive of the cost of financing, the governing board must adopt a resolution authorizing the political subdivision to enter into an installment purchase contract with the successful bidder or offerer or making a bid or offer inclusive of the cost of financing.

If the Board determines that it is in the best interest of the political subdivision to select a bid, offer or proposal, as the case may be, exclusive of the cost of financing, it must adopt a resolution requiring the capital improvement to be procured from the successful party making a bid, offer or proposal, exclusive of the cost of financing, and directing that non-vendor financing be obtained pursuant to the State Comptroller's applicable regulations. Such resolution must also authorize the political subdivision to enter into an installment purchase contract with any party selected to provide the financing (or, if certificates of participation are to be issued, with a party acting on behalf of the holders of the certificates of participation, the resolution may also delegate to the chief fiscal officer the power to cause certificates of participation to be sold pursuant to the State Comptroller's applicable regulations.

Any such resolution adopted must include a statement that execution of the installment purchase contract will not cause the political subdivision to exceed the limits prescribed by paragraph c of subdivision 6 of Section 109-b of the General Municipal Law.

Public sale of certificates of participation. A political subdivision is permitted to cause certificates of participation issued in connection with one or more of its installment purchase contracts to be sold at public sale, although, this has rarely been done in this State. Such certificates of participation must be sold to the bidder offering the lowest interest cost as computed in accordance with the net interest cost method, taking into consideration any premium or discount, or the actuarial or true interest cost method, whichever is specified in the notice of sale. The notice of such sale must be circularized in accordance with any rule or order prescribed by the State Comptroller pursuant to paragraph d of Section 57.00 of the LFL for the circularization of notices for the sale of bonds. Where the notice of sale provides that bids shall be awarded based on net interest cost, the notice shall also require that the interest rate for each maturity shall not be less than the interest rate for any prior maturity. The notice of sale must be circularized not fewer than four (4) nor more than fifteen (15) days, Sundays excepted, before the date fixed for the public sale unless the notice provides for a supplemental notice of sale in accordance with the procedure for the sale of bonds in paragraph(d) of Section 58.00 of the LFL.

Private sale of certificates of participation. The Board or the chief fiscal officer, if the Board has delegated such power to him, may determine that a public sale of certificates of participation is not in the best interests of the political subdivision. The determination of the governing board or chief fiscal officer, as the case may be, shall state that a private sale of such certificates of participation is expected to reduce the cost of financing and set forth the specific factors upon which the governing board or chief fiscal officer has relied on making such determination. The factors recited in such determination may include:

a. unstable or volatile market conditions;
b. conditions of fiscal stress or negative credit factors being experienced by the issuer;
c. the large dollar amount of the proposed issue;
d. the complexity of the issue; or
e. any other factor which the governing board or chief fiscal officer, as the case may be, reasonably and in good faith believes will cause the cost of financing to be lower if the certificates of participation are sold at private rather than public sale.

Such determination, if made by the governing board, shall be made by resolution and if made by the chief fiscal officer, shall be made in a certificate filed with the governing board prior to such sale. Upon making the determination required, such certificates of participation may be sold at private sale, provided that any underwriters, providers of letters of credit or liquidity facilities, bond counsel and financial advisors to be used in connection with such sale have been selected in accordance with the policies and procedures contained in the applicable State Comptroller's regulations. The prior approval of the State Comptroller is not required for private sale of certificates of participation conducted in accordance with these requirements.

Solicitation of alternative financing quotations. The governing board, or if authorized by the governing board, the chief fiscal officer may solicit alternative quotations for financing from qualified interested parties. The political subdivision or chief fiscal officer, as the case may be, is to prepare and maintain written documentation of compliance with this section, including the names and addresses of all qualified interested parties from which financing quotations were sought, the responses received from such parties and written justification of the ultimate selection made. Any political subdivision which enters into an installment purchase contract by private sale cannot permit certificates of participation to be issued in connection therewith except as part of a pooled or aggregate program.

Application of periodic payments and proceeds of certificates of participation. Periodic payments to be made under an installment purchase contract and the proceeds of certificates of participation shall only be applied towards the following:

a. the cost of the capital improvements being financed;
b. the payment of interest pursuant to paragraph (e) of subdivision 2 of the General Municipal Law, section 109-b;
c. preliminary costs of surveys, maps, plans, estimates, taking of title and interest during construction;
d. the establishment of reserve funds;
e. the cost or premiums of letters of credit, insurance or other credit enhancements;
f. the costs of bond counsel, financial advisors, underwriters, trustees and paying agents; and
g. other actual and necessary expenses directly related to the issuance of certificates of participation or execution of the installment purchase contract.

The political subdivision must include in its annual report filed with the State Comptroller in accordance with Section 31 of the General Municipal Law such information as the Comptroller may require for all installment purchase contracts and certificates of participation that are issued in connection with such installment purchase contracts, including the amount and date of all certificates of participation sold at private sale.

Energy Performance Contracts

Installment purchase contracts tied to energy performance contracts are also subject to the rules provided in Section 109-b of the General Municipal Law but as modified by the requirements of Article 9 of the Energy Law. They are specialized form of installment purchase contract for capital projects designed to reduce energy costs and involving guaranteed savings.

The term "energy performance contract" is defined in Section 9-102(4) of the Energy Law as:

> [A]n agreement for the provision of energy services, including but not limited to electricity, heating, ventilation, cooling, steam or hot water, in which a person agrees to install, maintain or manage energy systems or equipment to improve the energy efficiency of, or produce energy in connection with, a building or facility in exchange for a portion of the energy savings or revenues.

The purpose of this law is to obtain long-term energy and cost savings for agencies and municipalities by facilitating prompt incorporation of energy conservation improvements or energy production equipment, or both, in connection with buildings or facilities owned, operated or under the supervision and control of agencies or municipalities, in cooperation with providers of such services and associated materials from the private sector. Such arrangements are believed by the State to improve and protect the health, safety, security, and welfare of the people of the state by promoting energy conservation and independence, developing alternate sources of energy, and fostering business activity.

The primary operative provision of law is Section 9-103 of the Energy Law:

> **Section 9-103 Energy Performance Contracts**
>
> 1. Notwithstanding any other provision of law, any agency, municipality, or public authority, in addition to existing powers, is authorized to enter into Energy performance contracts of up to thirty-five years duration, provided, that the duration of any such contract shall not exceed the reasonably expected useful life of the energy facilities or equipment subject to such contract.
>
> 2. Any energy performance contract entered into by any agency or municipality shall contain the following clause: "This contract shall be deemed executory only to the extent of the moneys appropriated and available for the purpose of the contract, and no liability on account therefore shall be incurred beyond the amount of such moneys. It is understood that neither this contract nor any representation by any public employee or officer creates any legal or moral obligation to request, appropriate or make available moneys for the purpose of the contract."
>
> 3. In the case of a school district or a board of cooperative educational services, an energy performance contract shall be an ordinary contingent expense and shall in no event be construed as or deemed a lease or lease purchase of a building or facility, for purposes of the education law.

4. Agencies, municipalities, and public authorities are encouraged to consult with and seek advice and assistance from the New York State energy research and development authority concerning energy performance contracts.

5. Notwithstanding any other provision of law, in order to convey an interest in real property necessary for the construction of facilities or the operation of equipment provided for in an energy performance contract, any agency, municipality or public authority may enter into a lease of such real property to which it holds title or which is under its administrative jurisdiction as is necessary for such construction or operation, with any energy performance contractor, for the same length of time as the term of such energy performance contract, and on such terms and conditions as may be agreeable to the parties thereto and are not otherwise inconsistent with law, and notwithstanding that such real property may remain useful to such agency, municipality or public authority for the purpose for which such real property was originally acquired or devoted or for which such real property is being use.

6. In lieu of any other competitive procurement or acquisition process that may apply pursuant to any other provision of law, an agency, municipality, or public authority may procure an energy performance contractor by issuing and advertising a written request for proposals in accordance with procurement or internal control policies, procedures, or guidelines that the agency, municipality, or public authority has adopted pursuant to applicable provisions of the state finance law, the executive law, the general municipal law, or the public authorities law, as the case may be.

7. Sections one hundred three and one hundred nine-b of the general municipal law shall not apply to an energy performance contract for which a written request for proposals is issued pursuant to subdivision six of this section.

This provision establishes the basic features of an installment purchase contract for energy savings equipment: the useful life ("PPU"), the contingent nature of the political subdivision obligation to pay, the method of procurement, the need for there to be savings guaranteed in the contract for the provisions to apply.

It was further clarified in 1996 by counsel to the New York State Energy Research and Development Authority that the financing portion of an energy performance contracting transaction may benefit from the same rules applicable to the acquisition of equipment through the lease purchase acquisition agreement portion. (This remains ambiguous in the law as written.)

As was pointed out at that time, for those who are considering energy performance contracting, the agreement to install, maintain, or manage energy systems or equipment must be "in exchange for a portion of the energy savings or revenues." Energy Law, Section 9-102(4). An energy performance contract should not be misused in an attempt simply to purchase equipment without regard to energy savings and without regard to other supporting services, such as maintenance, monitoring, and other activities that are necessary to ensure energy savings.

In Summary,

a. Energy performance contracts with vendor financing may be entered validly into by municipalities and school districts (and school districts may do so without the usually mandatory voter approval but this is not free from doubt.)

b. Third-party financing for an energy performance contract may be validly entered into by municipalities and school districts (and school districts may do so without voter approval but this is not free from doubt) and certain other relevant elements of General Municipal Law Section 109-b should also be complied with.

c. Energy performance contracts may be entered into only for equipment and incidental reconstruction costs in connection therewith, *not* for integral structural elements such as roofs and windows, and internal elements such as wall insulation and asbestos removal.

d. The installment purchase agreements entered into in connection with an energy performance contract should comply with the level annual debt service rules of the LFL, in accordance with the requirements of General Municipal Law Section 109-b applied to the financing portion of the transaction (but not to the energy performance contract portion).

e. A political subdivision could adopt a bond resolution for the purchase and installation of energy-saving equipment (complying in such case with voter referendum requirements) and in conjunction therewith enter into an energy performance contract as a service contract with a guaranteed savings provision. However, as the serial bonds or bond anticipation notes would be payable regardless of savings, and would not be subject to a non-appropriation clause, the energy performance contract would require drafting to account for such structure (unlike the cases of vendor financing or third-party institutional financing both of which are subject to a non-appropriation clause). For example, such an energy performance contract would require not only savings and penalties for the lack thereof, but also a termination/liquidated damages provision for payment to the municipality in the event of non-appropriation and/or cancellation, in order for the municipality to pay off its general obligation debt. Also, any "savings" projected (and achieved) in an energy performance contract must be net of any State aid for the project. Such debt would need an early redemption provision.

f. The direct applicability of these rules to buildings owned by Public Library Districts is not know. If the library building is owned by a school district or municipality, then it would seem reasonable that the Affiliated Entity can enter into an energy performance contract for the building.

CHAPTER EIGHTEEN

Bond Insurance and Section 168.00 of the Local Finance Law

A legislative body is authorized and empowered by Section 168.00 of the LFL to enter into agreements (and delegate to the chief fiscal officer authority to do so) as it deems reasonable and appropriate, with any department or agency of the United States of America, the State, or any other financially responsible party, to facilitate the issuance, sale, resale and payment of bonds, notes, or other evidences of indebtedness, including, but not limited to letters of credit, lines of credit, revolving credit, bond insurance or other credit enhancements. Such agreements may provide for (i) the advance or advances of funds on behalf of such public body to pay the interest on and principal and premium of bonds, notes or other evidence of indebtedness on their date or dates of maturity or redemption or when interest is otherwise due, and for (ii) the reimbursement of such advance or advances.

Before the great credit meltdown of 2008, bond insurance was often utilized in bond issues and the major insurance companies providing bond insurance for general obligation and revenue bond issues in New York State were Ambac Indemnity Corporation ("AMBAC"), Financial Guaranty Insurance Company ("FGIC"), MBIA Corporation ("MBIA"), Financial Security Assurance, Inc., ("FSA") and CIFG Assurance. Losses due to insuring collateral mortgage obligations and subsequent ratings downgrades made most bond issuers unable to sell bond insurance that would save the issuer money on the interest cost. Now, in 2010 the market is redeveloping and the players have changed, to some extent: Assured Guaranty Municipal Corporation, Municipal and Infrastructure Assurance Corporation, Everspan Financial Guaranty Corporation (formerly AMBAC), and National Public Finance Guarantee Corporation (owned by MBIA) are the emerging bond insurers for school district and municipal debt. Whether a serial bond issue should be insured is a financial question: Will it save the Library District money on the interest rates the Library District will have pay to the holders of the Affiliated Entity debt? In competitive bond sales, it is generally the purchasing broker-dealer who decides whether to buy bond insurance (and pays for it out of any expected profits from resale of the debt). In a negotiated bond transaction, it is the issuer (*i.e.*, the Affiliated Entity or a free association library) which decides (and pays the premiums which Section 168.00 of the LFL permits to be treated as part of the cost of the object(s) or purpose(s) being financed by the bonds), usually with the help of a financial advisor. The balance sheet and the bond rating help make this determination.

It is common for a financial advisor to run anticipated debt service schedules at anticipated insured and uninsured rates to assist in making this determination.

Bond anticipation notes are not subject to the bond insurance option although they can be sold with a letter-of-credit purchased from a bank which as a credit enhancement. As this is very rare in New York State for note issuers it will not be further discussed in this primer.

If it is the issuer which is determining to acquire (and pay for) bond insurance, the issuer must take the following considerations into account pursuant to Section 168.00 of the LFL:

"1. consider the ability of the credit or liquidity enhancement provider to make required payments as and when due under the terms of the appropriate governing instruments;
2. consider the business reputation of the credit or liquidity enhancement provider;
3. consider the maximum term of the credit or liquidity enhancement relative to the maturity of the bonds, notes or other obligations being credit or liquidity enhanced;
4. provide for the right of substitution for the credit or liquidity enhancement provider in all agreements, including a provision permitting such substitution when the rating of the credit or liquidity enhancement provider falls below the probable credit rating of the issue without considering the credit or liquidity enhancer; and
5. consider the cost of the credit or liquidity enhancement relative to the savings or other benefit likely to be achieved through the utilization of the credit or liquidity enhancement."

CHAPTER NINETEEN

Financing for School District Affiliated Public Libraries—Commonly Asked Questions

Public Libraries are the step-children of their related school district. They seem to be independent political subdivisions of the State. They have the power to tax. And yet they cannot issue their own general obligation debt. (Remember, a mortgage note is not general obligation debt.) And therein lies an often difficult situation.

This chapter is written to answer certain questions frequently raised by school district and public library administrators, board members and their legal counsel about general obligation financing of public library capital projects of school district affiliated public libraries. (*See also*, Chapter 21 on Dorm financings and Chapter 9 on mortgage note financings)

Is the School District obligated to hold a special district meeting to approve a proposition for a public library capital improvement and the issuance of School District obligations therefor at the request of the Library Board of Trustees?

Yes.

Where a Library Board of Trustees requests an appropriation proposition to be placed on a school district ballot, the Board of Education is obligated to comply pursuant to Section 259 of the Education Law. *George F. Johnson Memorial Library v. Springer*, 11 A.D. 3rd 804 (2004); Op. St. Compt. 81-167. Likewise, for a capital improvement, pursuant to Section 260(9) and (10) of the Education Law in an amount sufficient to raise the annual Library budget levy by the maximum estimated annual debt service on obligations to be issued for the capital improvement. Ops. State Compt. 79-474, 80-154, 80-807.

Who pays for the expense of calling a special district meeting to vote upon a library capital project?

According to Op. Atty. Gen. (Inf) 69 (1974), these are expenses to be paid by the school district. *See also Bean v. Board of Education* 71 Misc2d 747 (1972), 336 N.Y.S.2d 703 (1972). Likewise, Op. St. Compt. 71-613 (unreported). However, according to the current text of Section 260(11) of the Education Law, the "cost of all such meetings and registrations shall be a charge to the library." The language seems unequivocal.

Is the School District obligated to issue its debt obligations for a public library district capital project approved by the voters of the library district?

Yes. The School District Board of Education must adopt a valid bond resolution after a successful referendum to implement the vote. And if they were to fail to do so? Don't ask. You don't need the aggravation. Education Law Section 260(10).

Who is responsible for site selection for a new library building?

While it is the Board of Education of the School District which has the power to acquire the site and hold title (unless the Library is purchasing the land with non-bond proceeds), it is the Board of Trustees of the Library which has the power of site selection and determination of suitability. *Matter of Appeal of the Board of Trustees, South Huntington Public Library*, 5 Educ. Dept. Rep. 158 (1966), 9 Op. St. Compt. 428 (1953).

Who is responsible for employing the architect?
Who is responsible for letting contracts and making purchases as authorized by the proposition?

Following the conclusions set forth in Opinion No. 6448 of the State Comptroller, 9 Op. St. Compt. 428 (1953) (*See, Also*, 1 Op. Counsel Edu. Dept. No. 83), the School District is responsible for employing the architect and for letting the necessary contracts for site acquisition, for the construction (or reconstruction) and for the purchase of furnishings and equipment. (Nevertheless, it is often the case that a Library Board of Trustees hires an architect in the first place, to prepare preliminary plans before it is able to determine whether to proceed with the project and ask the School District to hold an election.) A Library Board is authorized to "approve plans" and a Library Board is authorized "to select the architect." *See* Section 260(10) Education Law.

It must be remembered that while the Library Board of Trustees maintains the Library building, if bond-financed, the building is owned by the School District and thus it has an interest in the design of the building. *See* Op. St. Compt. 82-127 in Chapter Nine for the applicability of State Education Dept. and school district approval of the plans and specifications for a library building.

Who should have control over the expenditure of the proceeds of obligations issued by the School District for the purpose of constructing (or reconstructing) the library building?

As a general rule, Section 259(1) of the Education Law provides that "all moneys received from taxes or other public sources for library purposes" be kept in a separate library fund by the School District and be expended only under direction of the Library Board of Trustees on "properly authenticated vouchers." The voucher system has caused considerable problems.

In 1973, Section 259 was amended to clarify that "all moneys received from taxes or other public sources" optionally could be paid over to the Library Treasurer upon written demand of the

Library trustees to the School District Board. As was noted in the legislative history of Chapter 200 of the Laws of 1973 by the State Education Department: "The proposed amendment would make the detailed accounting of library funds the responsibility of the library board." The State Education Department also pointed out:

> "With the law requiring that the school treasurer maintain the funds but that the library trustees direct the expenditure by means of vouchers, there is a constant dispute as to who should keep the detailed accounting records and who should be responsible for this expense. Due to this dispute school district auditors often have a difficult time locating records since both boards may deny their responsibility for keeping them. Another problem occurs when boards of education attempt to control the management of the library by directing their treasurer to refuse to approve properly authenticated vouchers for policy reasons. Another dispute arises over who is entitled to the interest from funds held by the school district treasurer for the library.
>
> The intent of this bill was to make the trustees of public libraries entirely responsible for the expenditure and therefore the maintenance of records of the funds raised for library purposes. Our Division of Library Development requires annual financial statements and would therefore be able to oversee the expenditures by public libraries."

Furthermore, Section 255 of the Education Law previously read:

> "Any such municipality or [school] district may acquire real or personal property for library purposes by gift, grant, devise, bequest or condemnation and may take, buy, sell, hold and transfer either real or personal property and administer the same for public library purposes."

This was also amended over twenty-five years ago to specifically eliminate the words "and administer the same," with the same intent to permit a library board of trustees to directly administer same instead of the school district.

Opinion of the State Comptroller No. 83-32 states that where a public library has appointed a library treasurer and such library board of trustees demands in writing that all so-described library moneys be turned over to such officer, a school district may be relieved of its responsibility as the custodian of the public library funds. Opinion 91-57 of the State Comptroller noted that "the ultimate control of the use, disposition and expenditure" of Library moneys is vested in the library board of trustees. Incidentally, Opinion of the State Comptroller 2002-7 has held that a library board of trustees may determine to accumulate library fund moneys for capital purposes and expend same without referendum.

According to an Opinion of the Attorney General, control over the disbursement of the *proceeds of bonds* issued for construction (or reconstruction) of the library building is with the School District, since it is the duty of the school district to provide such building for public library purposes. (1953 Opin. Atty. Gen. 141; however, the statute has been revised since that opinion as described above.) Likewise predating the 1973 amendments but focused on bond proceeds, Opinion 66-728 of the State Comptroller holds that such bond proceeds are to be disbursed by the chief fiscal officer of the school district in payment of claims audited and ordered paid by the board of education.

In summary, the analysis that applies to "all moneys received from taxes or other public sources" *may not* apply to the proceeds of obligations issued by the school district for the construction or reconstruction of a library building. The obligations are those of the school district and the school district must retain some control over the disbursement of the proceeds thereof in order to (among other things) make sure that such disbursement is not in contravention of the Federal arbitrage regulations and that the requisite arbitrage rebate payments are paid to the Internal Revenue Service, if necessary.

The best practical answer here is for the two parties to work out an intermunicipal agreement that can meet both parties needs. Model documents for this do exist and have actually worked!

Who is responsible for the payment of debt service on obligations issued by the School District for the purpose of construction or reconstruction of a public library building "on behalf of" a Public Library Board of Trustees?

Since the obligations are those of the School District, and it is the School District which is responsible for paying debt service thereon, this debt service, both principal and interest is to be included in the school budget, rather than the library budget (see Opinion 70-440 of the State Comptroller and 12 Op. St. Compt. 265 (1956) (also 1962 Op. St. Compt. 62-978 (unreported) and 1963 Op. St. Compt. 63-195 (unreported) to same effect)). However, in recent years, several school districts and their public libraries have worked together to include such moneys in the library budget and levy pursuant to innovative contractual arrangements. Such arrangements have both practical and legal considerations. In any event, it is the library budget and levy that the library district voters elect to increase to cover debt service on the library project. The law is clear on this point.

In this regard, it is worth noting that Section 259 of the Education Law states that in the case of a school district, "the appropriation for library purposes shall be submitted to the voters of the district in a separate resolution and shall not be submitted as part of the appropriation of the necessary funds to meet the estimated expenditures of the school district." This view has been supported in interpretation by the State Comptroller's Office in 19 Op. St. Compt. 124 (1963). It is the opinion of the Education Department that the Board of Education has no discretion in the matter. Op. Counsel Educ. Dept. No. 8 (1951); Educ. Dept. Rep. 172 (1990). In 50 Op. St. Dept. 507 (1935) the Education Department offered this opinion:

> "It is, therefore, the duty of the collector of the school district to collect two budgets—one voted by the school district for school district purposes, and the other voted by the library district for the library purposes. Many collectors combine the two

> budgets and send one tax bill to the taxpayer. Other collectors separate the two, sending but one bill but indicating thereon the amount due for school district purposes and the amount due for library purposes. The latter procedure undoubtedly comes closer to complying with the intent of the provisions of section 1122 of the Education Law. However, in either case, it is the duty of the collector to segregate and keep separate the amount of money collected for the school district and the amount of money collected for the library district."

Remember: Public libraries are without authorization in current law to directly issue indebtedness in their own name either for capital purposes or in anticipation of the receipt of tax revenues (TANs), (other than a mortgage note in accordance with Opinions of the State Comptroller 82-127, and 76-771 and Opinion of the Education Dept. Op. St. Dept 509 (1935).)

Who owns a public library building?

According to Opinions of the State Comptroller and the Education Department's Office of Counsel, title to a library building is vested in a school district but the building is in possession and control of the Library Board of Trustees while it is used as a library. 4 Op. St. Compt. 609 (1948) and Op. Counsel Educ. Dept. No. 83 (1953) (provided, however, to the extent real property is acquired in part with moneys received by a library as a gift or bequest, title may be held jointly. 9 Op. State Compt. 142 (1953)).

Upon cessation of use as a library, it is the right of the school district to sell the property pursuant to the standard procedures for the sale of school district property. Op. Counsel Educ. Dept. No. 83 (1953). This follows from the school district holding title to the property.

A building acquired without school district moneys in wholly the property of the library district. 32 Op. State Compt. 30 (1976), 32 Op. State Compt. 105 (1976).

Who is responsible for major repairs to a public library building?

According to Opinions of the State Comptroller (80-361 and 15 Op. St. Compt. 14 (1959), such repairs may be paid from the library fund, or, in the discretion of the school board, from school district operating moneys.

Can a public library district ask a school district to issue TANs on its behalf?

Yes, and in Opinion 92-28 of the Office of the State Comptroller it was held that the interest expense is a charge of the School District, which the Library District may choose to reimburse.

Have the interpretations of the State Comptroller and Attorney General if dated before 1973 noted above been made obsolete by the later amendments of the Education Law?

That remains undetermined, making a conservative approach essential.

Do these interpretations apply to Library Districts with an Affiliated Entity other than a School District?
We think so. Probably. Seems logical, doesn't it?

See why we noted at the outset that public libraries were step-children?

CHAPTER TWENTY

Capital Financings For Free Association Libraries

If a public library is the stepchild of its Affiliated Entity, a free association library is an orphan. But it is a very strange orphan with special powers. They are definitely *not* political subdivisions. They cannot issue general obligation debt. They do not have independent taxing power so they cannot pledge the general obligation unlimited taxing power. And yet, if they have a district context, they can compel (with supporting petition) an Affiliated Entity which is a political subdivision of the State with taxing powers to increase the free association library budget through a public vote if the library trustees are publicly elected. How odd is that? Very.

Can a free association library holding corporate status as an education corporation or as a not-for-profit corporation (which under Section 216 of the Education Law, the Regents must also authorize) under New York State Law actually have tax-exempt debt issued on its behalf? Yes, it can. But not by its Affiliated Entity!

Most people think of local governmental bonds and notes as strictly the domain of counties, cities, towns, villages, school districts and fire districts. By and large, this is true. Only political subdivisions of the State have the power to levy a tax to pay debt service on obligations and thus only political subdivisions can issue "general obligation" bonds and notes as described in Chapter 1 of this primer, which contain the pledge of the local government's "faith and credit." A free association library is not able to pledge to levy a tax in that manner but it can pledge its receipt of any particular stream of revenues. These type of bonds are known generically as "revenue bonds."

A not-for-profit free association library can, in fact benefit from the issuance of debt obligations that are *not* "general obligations," yet are able to offer investors interest that *is* tax-exempt for federal income tax purposes, thereby lowering the library's borrowing cost. How is that? It is the result of one provision in the Internal Revenue Code of 1986 and certain provisions in the not-for-profit law and education law of the State. The not-for-profit corporation law is applicable to a domestic educational corporation such as a free association library to the extent stated in Section 216-a of the Education Law. It is not subject to the Local Finance Law.

The following discussion is related to tax-exempt debt issued on behalf of a free association library. Such libraries could also issue a mortgage note. *See* Chapter 9, "Mortgage Notes of a Library District" for more on this option.

Section 145

The federal tax law provision is Section 145 of the Code which reads as follows:

SECTION 145 QUALIFIED 501 (C) (3) BOND.

(a) In General.—For purposes of this part, except as otherwise provided in this section, the term "qualified 501(c)(3) bond" means any private activity bond issued as part of an issue if—

(1) all property which is to be provided by the net proceeds of the issue is to be owned by a 501(c)(3) organization or a governmental unit, and

(2) such bond would not be a private activity bond if -

(A) 501(c)(3) organizations were treated as governmental units with respect to their activities which do not constitute unrelated trades or businesses, determined by applying section 513(a), and

(B) paragraphs (1) and (2) of section 141(b) were applied by substituting "5 percent" for "10 percent" each place it appears and by substituting "net proceeds" for "proceeds" each place it appears.

(b) $150,000,000 LIMITATION ON BONDS OTHER THAN HOSPITAL BONDS.—

(1) In General.—A bond (other than a qualified hospital bond) shall not be treated as a qualified 501(c)(3) bond if the aggregate authorized face amount of the issue (of which such bond is a part) allocated to any 501(c)(3) organization which is a test-period beneficiary (when increased by the outstanding tax-exempt nonhospital bonds of such organization) exceeds $150,000,000.

(2) Outstanding Tax-Exempt Nonhospital Bonds.—

(A) In General.—For purposes of applying paragraph (1) with respect to any issue, the outstanding tax-exempt hospital bonds of any organization which is a test-period beneficiary with respect to such issue is the aggregate amount of tax-exempt bonds referred to in subparagraph (B).

(i) which are allocated to such organization, and

(ii) which are outstanding at the time of such later issue (not including as outstanding any bond which is to be redeemed (other than in an advance refunding) from the net proceeds of the later issue).

(B) Bonds Taken Into Account.—For purpose of subparagraph (A), the bonds referred to in this subparagraph are—

(i) any qualified 501(C)(3) bond other than a qualified hospital bond, and

(ii) any bond to which section 141(a) does not apply if-

(I) such bond would have been an industrial development bond (as defined in section 103(b)(2), as in effect on the day before the date of the enactment of the Tax Reform Act of 1986) if 501(c)(3) organizations were not exempt persons, and

(II) such bond was not described in paragraph (4), (5), or (6) of such section 103(b) (as in effect on the date such bond was issued).

(C) Only Nonhospital Portion of Bonds Taken Into Account.—

(i) In General.—A bond shall be taken in account under subparagraph (B) only to the extent that the proceeds of the issue of which such bond is a part are not used with respect to a hospital.

(ii) Special Rule.—If 90 percent or more of the net proceeds of an issue are used with respect to a hospital, no bond which is part of such issue shall be taken into account under subparagraph (B)(ii).

(3) Aggregation Rule.—For purposes of this subsection, 2 or more organizations under common management or control, shall be treated as 1 organization.

(4) Allocation of Face Amount of Issue; Test-Period Beneficiary.—Rules similar to the rules of subparagraphs (C), (D) and (E) of section 144(a)(10) shall apply for purposes of this subsection.

(5) Termination of Limitation.—This subsection shall not apply with respect to bonds issued after the date of the enactment of this paragraph as part of an issue 95 percent or more of the net proceeds of which are to be used to finance capital expenditures incurred after such date.

Got that? Ok, here's what it means:

If your free association library has Section 501(c)(3) tax status and it wants to borrow no more than $150,000,000 for a library-owned, library-operated addition (for example) (difficult I know, but you'll have to manage within that maximum), and the borrowed money will only to go good mainstream library functions (e.g. no unrelated manufacturing subdivision in the basement, no massage parlor, no bakery café), then you got a deal!

Who Can Issue The Debt

Generally, only state or local governmental entities and public benefit corporations, agencies or authorities which are not themselves political subdivisions are eligible actually to issue tax-exempt bonds (the "Issuer"). The nonprofit corporation borrows the proceeds of tax-exempt bonds issued by such an Issuer which is not a political subdivision at the request of the nonprofit corporation. One such typical issuer might be your local Industrial Development Agency ("IDA") if the authority for an IDA to issue debt on behalf of not-for-profit corporations is reinstated by the state legislature, or if special legislation is enacted granting such powers to your local IDA for your project.

In most cases, a non-profit corporation cannot itself directly issue *tax-exempt* debt. It *can* directly issue debt (e.g. a mortgage note), but the interest would be federally taxable. Tax-exempt financings with bond issuance directly by a not-for-profit pursuant to either Revenue Rulings 57-128 or 63-20 which may be possible are somewhat complicated. Consult bond counsel to learn more about how these financings work.

Section 501(c)(3)

In order to be eligible to borrow using tax-exempt bonds, a nonprofit corporation must be a so-called "501(c)(3) corporation," meaning a nonprofit corporation that has received a determination letter from the Internal Revenue Service that it qualifies as an organization of the type described in Section 501(c)(3) of the Internal Revenue Code. Two other types of nonprofit corporations are eligible to use tax-exempt bonds: (1) an "instrumentality" of a governmental entity as described in IRS Revenue Ruling 57-128 (which involves a good deal more control by the governmental entity than is the case in most 501(c)(3) corporations and (2) a so-called "63-20 corporation," which is a nonprofit corporation considered to be acting on behalf of a governmental entity in accordance with the requirements of Revenue Ruling 63-20 as updated by Revenue Procedure 82-26, including a requirement that any property financed by the 63-20 corporation vests in the governmental entity at the end of the term of the bonds. These types of nonprofit corporations are often established specifically to facilitate structuring of a tax-exempt financing and do not require a ruling or determination from the IRS (although some do also obtain a 501(c)(3) determination). A 63-20 corporation is the only type of nonprofit corporation that can itself issue tax-exempt bonds without having to apply to a public entity like an Industrial Development Agency to do so.

Section 501(c)(3) generally contemplates nonprofit corporations organized and operated for one or more of the following purposes: scientific, testing for public safety, literary, educational or prevention of cruelty to children or animals. These purposes are fairly broadly defined in the Code. There are approximately one million 501(c)(3) nonprofit corporations in the United States, and some of them are libraries.

So, you see, under federal tax law if your library meets the requirements of being qualified as a Section 501(c)(3) organization as described above, then debt issued by or on behalf of the association will be treated like the obligation of a political subdivision like a town or a village, or a school district. That is to say, the interest paid on it to buyers (like banks) of your debt will not be taxed on their federal income tax returns. Thus, the interest rates that the library will need to pay to them to loan you money on any notes or bonds issued will be *lower than*, for example, a commercial bank loan, a mortgage note, or an ordinary installment purchase agreement.

Relevant State Law

The relevant sections of the State not-for-profit law are Article 2 and Article 5 which states in relevant portions:

"**Section 202.** General and special powers:

(a) Each corporation, subject to any limitations provided in this chapter or any other statute of this state or its certificate of incorporation, shall have power in furtherance of its corporate purposes....

(4) To purchase, receive, take by grant, gift, devise, bequest or otherwise, lease, or otherwise acquire, own, hold, improve, employ, use and otherwise deal in and with, real or personal property, or any interest therein, wherever situated.

(5) To sell, convey, lease, exchange, transfer or otherwise dispose of, or mortgage or pledge, or create a security interest in, all or any of its property, or any interest therein, wherever situated....

(9) To make contacts, give guarantees and incur liabilities, borrow money at such rates of interest as the corporation may determine, issue its notes, bonds and other obligations and secure any of its obligations by mortgage or pledge of all or any of its property or any interest therein, wherever situated....

(16) To have and exercise all powers necessary to effect any or all of the purposes for which the corporation is formed."

"**Section 506.** Bonds and security interests.

(a) No corporation shall issue bonds except for money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the corporation shall be conclusive.

(b) A corporation may pay reasonable interest on its bonds, may issue its bonds at a reasonable discount and may pay a reasonable premium for the redemption thereof prior to maturity, but the holders of its bonds shall not be entitled at any time to receive any part of the income or profit of the corporation nor at maturity to receive more than the principal sum thereof plus interest due and accrued thereon. In the absence of fraud in the transaction, the judgment of the board as to the reasonableness of any such interest, discount or premium shall be conclusive. However, with respect to bonds not a part of a public offering, notwithstanding the terms of the instrument, no member of a corporation shall be entitled to receive, directly or indirectly, as a holder or beneficiary of such bond, prior to maturity or redemption, more than simple interest thereon at a rate equal to the higher of (1) the maximum interest authorized pursuant to section 5-501 of the general obligations law or (2) one percent over the prime rate of interest generally prevailing on the interest due date in the Federal Reserve District of New York, nor at maturity or redemption, more than the principal sum thereof plus any interest, not exceeding the maximum interest herein specified, due and accrued thereon.

(c) A corporation may, in its certificate of incorporation or by-laws, confer upon the holders of any bonds issued or to be issued by the corporation, rights to inspect the corporate books and records and, upon default of interest or principal, to vote in the election of directors. The certificate of incorporation or the by-laws may apportion the number of votes that may be cast with respect to bonds on the basis of the amount of bonds held.

(d) The board may authorize any mortgage or pledge of, or the creation of a security interest in, all or any part of the corporation's personal property, or any interest therein.

Unless the certificate of incorporation provides otherwise, no vote or consent of the members shall be required to approve such action by the board."

This next section is specifically *excluded* from applicability to a "domestic educational corporation" as they have the separate authority of Education Law Section 226(6):

"**Section 509.** Purchase, sale, mortgage, and lease of real property.

No purchase of real property shall be made by a corporation and no corporation shall sell, mortgage or lease real property, unless authorized by the vote of two-thirds of the entire board, provided that if there are twenty-one or more directors, the vote of a majority of the entire board shall be sufficient."

These provisions authorize an organization organized under the not-for-profit corporation law to borrow under state law and include authority to borrow in the form of a mortgage note in addition to Section 501 (c)(3) notes or bonds. Do they apply to a free association library chartered by the State? Yes. A free association library is an "education corporation" chartered by the Board of Regents and has bestowed upon it all the power of a not-for-profit corporation pursuant to Section 216-a of the Education Law of the State.

Initial Steps To A Free Association Library Financing

Therefore, the first step in considering a free association library borrowing is to examine the company's Certificate of Incorporation or more likely, Charter from the State of New York Board of Regents, its constitution and its By-laws, as well as obtain a "Bring-Down Certificate" from the Secretary of State or the Board of Regents to confirm that the library's Certificate of Incorporation or Charter remains effective and that the association is thus a "subsisting corporation." (It has generally been found useful to be sure the entity borrowing the money actually exists; banks, in particular, are keen to be repaid after all the phantom borrowing that resulted in the 2008 credit crunch.)

Next let us look at the federal tax law requirements, on the assumption that the library is a viable not-for-profit holding Section 501(c)(3) status.

You will have noticed that Section 145 of the Code states that 501(c)(3) bonds are treated as "private activity bonds," i.e., they do not get simple treatment like any ordinary local governmental bond, as there are certain other Code provisions which are applicable to 501(c)(3) bonds that are not applicable to most debt of counties, cities, towns, villages, fire districts or school districts. You knew there was a catch right? This one is not difficult.

Section 147(f) of the Code requires (a) a public hearing be held and (b) approval by the local legislative body or chief executive thereafter prior to any debt issuance by the library. Even though it would be library debt, federal tax law requires that the local political subdivision which is likely the Affiliated Entity "approve" the debt. This approval does not make that political subdivision liable on the library debt in whole or any part. The wording and timing of the Notice of Public Hearing must comply with certain detailed requirements of U.S. Treasury Department regulations and part of the role of bond counsel is to ensure that the notice and the hearing are in compliance. It should be held prior to any public vote to increase the tax levy to cover the debt service.

Another federal tax law consideration at the outset of a financing is that you must be a qualified Section 501(c)(3) organization and that the capital improvement or item to be financed must be one that the tax law considers eligible for the federal tax exemption. Any library construction or reconstruction project or vehicles or equipment purchase is likely to qualify as eligible. Again, these are questions for bond counsel.

(One other federal tax law consideration for so-called "501(c)(3) bonds is the 2% costs of issuance rule: Costs incurred with issuing such bonds, such as underwriter's discount or fees, fees of bond counsel and other lawyers and consultants such as financial advisors, rating agency fees, bank trustee's fees, official statement printing charges and the like, may be included in the bond issue, subject to a cap of 2% of the bond issue, which cap does not include the cost of any bond insurance or credit enhancement. This 2% cap is usually more than enough to cover costs of issuance, unless the bond issue is relatively small in size or unusually difficult and time consuming to complete.

Interest payable on such bonds during the longer of three years or the period in which the project is to be constructed and for up to one year after completion of construction may be included (i.e., capitalized) in the bond issue (and not part of the 2% limit). The capitalized interest is generally held by the bond trustee and used to pay interest on the bonds, with the result that the nonprofit corporation does not have to pay any cash upfront for debt service on the bonds during such period.)

So, in a nutshell, if the free association library meets the requirements described in Section 145 quoted above and is a subsisting not-for-profit educational institution in New York State, with no restrictions as to debt issuance in its establishment or governing documents, then the library is in a position to consider debt issuance for its capital project or equipment. *Please Note:* If the library is able to issue debt through the local IDA (assuming IDAs are once again permitted to issue debt on behalf of not-for-profits, which authority has presently lapsed), or the Dormitory Authority the interest thereon will be tax exempt for federal income tax purposes. Interest on a mortgage note directly placed with a local bank as part of a "conventional loan" will not be tax exempt and thus it will be higher.

Next, we come to the critical juncture of finding a local bank, investment bank or other financial institution interested in purchasing your debt. Since a free association library is not a political subdivision, this is not as easy as it is for a school district, for example. Before even arranging for a public hearing, the library treasurer should contact local bankers, the local Industrial Development Agency (about which more is described below), the Dormitory Authority (*See* Chapter 21) and the local counsel about what may be possible. Bond counsel can also usually provide a list of contacts at regional investment banking firms that may have an interest in purchasing or privately placing this debt. Because a free association library does not have the general power of property taxation, bond purchasers may require a mortgage or other security interest on library property (even though in a real financial difficulty it would be hard to imagine a local bank as holder of a library bond foreclosing on a library building in order to recover its loaned money). If the library receives significant state aid, it may be able to pledge these moneys but keep in mind that such aid typically flows through the regional library system and this may require some special attention to get the pledge to be effective. Contractual payments from a political subdivision could be pledged as security for a free association library bond issue. If the borrowing is a significant amount, say $1,000,000 or over, it may be useful to have a financial advisor to help with the debt sale.

Industrial Development Authority Financings

As noted above, as a Section 501(c)(3) entity, you need to find a valid governmental entity that can issue debt on your behalf. One such entity, if the State Legislature reauthorizes the "civic facility" provision of Section 854 of the General Municipal Law, is your local Industrial Development Agency.

The basic steps in a free association library tax-exempt IDA financing are as follows:

1. Check the establishment proceedings and other documentation and the current by-laws for provisions on debt.
2. Check your basic documentation file also for your company's federal tax status. Are you a Section 501(c)(3) organization? Do you have a current contract with your Affiliated Entity (if required)?
3. Hire competent Bond Counsel. (Please note the word "competent.")
4. Ask the Secretary of State or Board of Regents, as applicable for a "bring-down" type certificate so you are sure of your current existent status.
5. Adopt a resolution requesting the local political subdivision which is your Affiliated Entity to hold a public hearing on your behalf and with your participation.
6. Hold a public hearing in conjunction with your local political subdivision on at least 14 days published notice. The notice must include: (a) a functional description of the project, including street address of building or location for equipment, (b) maximum estimated cost, (c) sources of funding, including amount of debt, and (d) the owner/operator of the project.
7. Adopt a resolution requesting the Affiliated Entity to hold a public referendum on an increase to the annual funding of the free association library sufficient to cover maximum anticipated debt service on any bonds issued for the capital project after discussion with your local IDA and its bankers about interest rates. (If you find anyone who can accurately predict interest rates in the future, please call us on our personal cell phones. We want to be their friend.)

8. Thereafter, obtain either a resolution of that political subdivision's legislative body or a certificate of their chief executive officer approving the issuance of the particular maximum amount of debt for the particular purpose, as described in the public hearing notice. Alternatively, the public vote may suffice for this purpose.
9. Adopt a resolution of your board of trustees by a simple majority vote to: (a) authorize the issuance of debt obligations in the particular maximum amount and for the particular purpose, (b) authorize the Chairperson and Treasurer of the association to sign necessary documentation to sell such debt, and (c) approve any needed security agreement such as a mortgage.
10. Begin discussions with local IDA on a timetable for debt issuance.
11. Hire competent financial advisor, if necessary.
12. Sell debt or place debt with purchasing bank, investment bank, other financial institution or very rich local residents.
13. Build new library additions; buy new mobile library truck.
14. Celebrate.

And, oh, yes, remember to budget to repay the loan. Please.

Dormitory Authority Financings

In addition to IDA financings (on hold as of this writing due to the lapse of authority for IDAs to issue debt on behalf of not-for-profits), and direct bank loans (not tax-exempt but also not subject to certain financing requirements noted above) a free association library can also finance through the Dormitory Authority of the State of New York. The initial steps will be the same as for an IDA financing. *See* Chapter 21 herein for further details on this method. The Dormitory Authority has existing generic legal authority to borrow on behalf of libraries including free association libraries. You will, however need special legislation to be named as a particular library authorized to utilize their services.

CHAPTER TWENTY-ONE

Debt Issued On Behalf of Libraries by the Dormitory Authority of the State of New York

The Dormitory Authority of the State of New York (hereinafter, "DASNY" or the "Dormitory Authority" or the "Authority") is authorized by Title 4 of the Public Authorities Law of the State to issue debt on behalf of institutions specifically authorized by the State Legislature. The Authority is a public benefit corporation of the State, created for the purposes of financing, and in some cases, constructing, a variety of public purpose facilities for certain educational, governmental and not-for-profit institutions. Section 1680 of the Public Authorities Law specifically includes "a public library" as an "educational institution" on whose behalf the Authority may issue debt.

In order for a particular library to be eligible for financing through the Dormitory Authority, the library must be covered by the Dormitory Authority Act, specifically §§ 1676 and 1680 of the Public Authority Law (the "PAL" or the "Act").

PAL § 1676(2)(b) defines "dormitory" to include "[a] public library." Odd, but there it is. PAL § 1676(32) goes on to define the term "public library" as "those libraries set forth in section five of the chapter of the laws of nineteen hundred ninety-three which added this subdivision [i.e., L.1993 c.672], as defined as a public library or as an association library pursuant to section two hundred fifty-three of the education law." Thus for a library to be eligible for DASNY financing, *it must be specifically included* by special legislation in this referenced section of law.

Likewise, PAL § 1680(1) defines "educational institution" to include "'[a] public library." Thus, PAL § 1680(3)(a), which authorizes the Dormitory Authority to "make loans to any educational institution for the acquisition, construction, [etc.]...of dormitories and attendant facilities," provides a statutory basis for the financing of public libraries. Moreover, PAL § 1680(33) gives a public library, subject to voter approval in accordance with the Education Law, "full power and authority to assign and pledge to the dormitory authority any and all public funds...in an amount sufficient to make all payments required to be made by such public library" pursuant to its loan agreement with the Dormitory Authority. Finally, to the extent required by the library's loan agreement with the Dormitory Authority, PAL § 1680(33) requires "all state and local officers...to pay all such funds so assigned and pledged" to the Dormitory Authority or the applicable bond trustee.

Again, as it is important to emphasize:

A library would need special legislation to be included in this definition.

To add a specific library to the Dormitory Authority Act, the Authority recommends the following language as a special act of the State Legislature:

AN ACT to amend chapter 672 of the laws of 1993, amending the public authorities law relating to the construction and financing of facilities for certain public libraries, in relation to expanding the list of eligible libraries to include [name of library].

§1. Section 5 of chapter 672 of the laws of 1993, amending the public authorities law relating to the construction and financing of facilities for certain public libraries, is amended to include [name of library] as an eligible public library for purposes of title 4 of article 8 of the public authorities law.

§2. This act shall take effect immediately

The above language designating the library as a "public library" for purposes of the Dormitory Authority Act not only confers the requisite statutory authorization on the Dormitory Authority, but it also authorizes, if applicable the pledge of tax revenues by the library and mandates the remittance of those revenues to the Dormitory Authority (or its bond trustee) by any state or local officers collecting them. The Dormitory Authority has financed about a dozen libraries, most of them school district public libraries as well as a few special district libraries and free association libraries.

Thus, a Public Library District does have the option to obtain financing with its Affiliated Entity or through a local mortgage note financing or through the Dormitory Authority, while a free association library has the option of mortgage note financing, IDA financing (if the "civic facility" option is re-authorized) or financing through the Dormitory Authority

Basic Structure of a Dormitory Authority Financing

In a Dormitory Authority financing, after adoption of a resolution or resolutions by the governing body of DASNY (the "DASNY Resolution") and other state approvals, the Authority issues its own bonds in order to raise funds to loan to the Library District and the Library District obligates itself to repay the loan and all costs of issuance.

A loan agreement between the Library District and the Dormitory Authority is most typically the basic document that sets out all of the details of the loan, its security and its repayment.

The description of a DASNY library transaction which follows is one common example of how such a deal works. There can be variations based on the particular facts and circumstances of any project.

Payment of the Authority Bonds—Nature of The Loan Agreement

Bonds issued on behalf of a library would be special obligations of the Authority payable solely from revenues, which would consist of certain payments to be made by the Library under a Loan Agreement with DASNY. The Loan Agreement will usually be a general obligation of the Library if it is a Public Library District and a contractual obligation if it is a free association library. Pursuant to the DASNY Resolution, these revenues, and the Authority's right to receive the revenues, are pledged to a bank acting as the trustee of the bonds issued by DASNY to raise the moneys to be loaned to the library (the "Trustee Bank"). The Trustee Bank uses such revenues to pay the DASNY bonds.

Before the Loan Authorization of Project, Payment and Tax Levy-Library Districts

As with Affiliated Entity debt for a Library District, a referendum must be held by the qualified voters in the Library District which authorizes the project and which includes the authority to enter into the Loan Agreement with DASNY to finance the project. The qualified voters must also authorize the Library to assign and pledge to the Authority funds in an amount sufficient to repay all obligations of the Library under the Loan Agreement, and authorize such funds to be raised by a real property tax assessment on real property located within the Library District to be levied annually for library purposes by the Library District. Thus, by referendum by the qualified voters in a Library District, the qualified voters must authorize the Library to (i) construct the capital project at a maximum estimated cost of $__________ and finance the capital project of the Library by borrowing an amount not to exceed $__________ through the issuance of bonds by the Authority, (ii) levy a tax within the Library District payable in annual installments in an amount not to exceed $__________ per year over a maximum pre-determined period of years, (iii) assign and pledge such tax to the Authority, and (iv) enter into any loan or mortgage agreement incidental to the foregoing. There are essential additional elements of any vote on library capital project that may utilize Dormitory Authority financing.

Security for the Library Bonds

Bonds issued by DASNY for your library will typically be secured in the first instance by the pledge and assignment to the Trustee Bank of the revenues and the security interest in such pledged revenues granted by the Library to the Authority under the Loan Agreement. Pursuant to the Loan Agreement, the Library covenants that the Authority's security interest in the pledged revenues will be a first lien thereon and will not be subject to any preexisting liens. The pledged revenues usually include all revenues and will usually consist primarily of real property taxes levied by the Affiliated Entity on behalf of the Library on all non-exempt real property in the Library District. The Real Property Tax Law and sometimes a local Tax Act govern methods and procedures to levy and collect real property taxes in the Affiliated Entity. Such Bonds will also be secured by all funds and accounts established for the bond issue with the Trustee Bank (with the exception of an arbitrage rebate fund).

The Library may be permitted to incur additional debt for the same or later projects secured by a parity lien (i.e. equal basis lien as opposed to a subordinate lien) on certain of the pledged revenues but only with the prior written consent of the Authority. A typical DASNY Resolution authorizes the issuance by the Authority, from time to time, to time, of bonds in one or more series, each such series to be authorized by a separate series resolution and to be separately secured from each other series of bonds. The holder of bonds of a series are not entitled to the rights and benefits conferred upon the holder of bonds of any other series.

The Bonds issued by DASNY for loan to your library will not be a debt of the Affiliated Entity nor will the Affiliated Entity be liable thereon in any regard nor under the Loan Agreement between the Library and DASNY.

The DASNY Bonds will not be a debt of the State nor will the State be liable thereon. DASNY itself has no taxing power. It is completely and solely depending on you to pay your obligation as set forth in the provisions of the Loan Agreement.

Thus, in summary, the DASNY Bonds will secured by the pledge and assignment to a Trustee Bank of the pledged revenues, the proceeds from the sale of Bonds themselves (until disbursed), all funds and accounts authorized and established under DASNY Resolution (with the exception of the arbitrage rebate fund) and the Authority's security interest in the pledged revenues.

Payment of DASNY Bonds—Control over certain Revenues of the Library District

The Bonds of DASNY issued for a library will be special obligations of DASNY secured by the revenues. The revenues typically consist of (i) required payments to be made by the library under the Loan Agreement to satisfy the principal and redemption price of and interest on the Bonds as further described herein and (ii) all amounts received as a consequence of enforcement of the Loan Agreement including amounts derived from the foreclosure or sale or realization upon the pledged revenues. The revenues and the right to receive them will be pledged to the Trustee Bank for the benefit of bondholders of the DASNY bonds issued for your library.

The Loan Agreement is a general obligation of the Library (in the technical sense for a Library District and in a more general sense for a free association library) and obligates the Library to make payments on account of the principal, redemption price of, and interest on outstanding bonds issued by DASNY in order to loan them to the Library. Such payments are typically to be made annually or semiannually on a fixed date(s) in an amount equal to the principal and interest (or if semiannually, then just interest on one such date) coming due on the next succeeding debt service due after the fixed date. The Loan Agreement also typically obligates the Library to pay, usually at least 45 days prior to a redemption date of bonds called early for redemption, the amount, if any, required to pay the redemption price of such bonds.

The Authority is authorized under the Act to direct State and local officers including without limitation, officers of the Affiliated Entity, to pay over to the Authority any and all public funds owed to the Library by the State or any political subdivision of the State in an amount sufficient to make all payments to be made under the Loan Agreement. In connection with the issuance of bonds, the Library, the Authority, the Affiliated Entity, a depository bank of the Library District (the "Depository Bank") and the Trustee Bank typically will enter into a Tax Pledge and Collection Agreement (the "Tax Pledge Agreement") governing the remittance and application of the annual tax levied against taxable real property within the Library District, and collected by the Affiliated Entity on behalf of the Library (the "Annual Tax"). Pursuant to the Tax Pledge

Agreement and for so long as DASNY Bonds remain outstanding, the Affiliated Entity, at the direction of the Library, will remit the Annual Tax to the Depository Bank. Note: Often *All of it!* This is known as a "lock box arrangement." Promptly upon receipt thereof, the Depository Bank will transfer an agreed upon percent thereof to the Trustee Bank for deposit in the Debt Service Fund for DASNY Bonds and the remainder thereof to the Library until such time as the sum of all receipts transferred by the Depository Bank to the Trustee Bank during such calendar year is equal to the aggregate debt service due on Library Bonds on the next succeeding aggregate annual debt service payment dates. The Tax Pledge Agreement may typically further provide, however, that if as of a certain date of any year, the sum of all receipts transferred by the Depository Bank to the Trustee Bank during such calendar year to said date is less than the aggregate debt service due on Library Bonds on the next succeeding aggregate annual debt service payment dates, the Depository Bank is required thereafter to transfer one hundred per cent (100%) of receipts thereafter received to the Trustee Bank for deposit in the Debt Service Fund until such time as the sum of all receipts transferred by the Depository Bank to the Trustee Bank during such calendar year is equal to the debt service due on DASNY Bonds issued for the library on the next succeeding aggregate annual debt service payment dates.

Additional Security for the DASNY Bondholders—The Mortgage

The Library's obligation to the Authority under the Loan Agreement is typically additionally secured by a mortgage on certain library property (the "Mortgaged Property") and security interests in certain fixtures, furnishings and equipment located herein or used in connection therewith. DASNY retains the authority, but usually has no intention to, assign the mortgage and such security interests to the Trustee Bank. Upon the happening of an event of default under the Resolution (other than a covenant default by the Authority which results in the interest on the Bonds no longer being excludable from gross income under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), the Authority is required to assign the mortgage and such security interests to the Trustee Bank. Unless the mortgage and such security interests are assigned to the Trustee Bank, neither the mortgage, the security interest in such fixtures, furnishings and equipment nor any proceeds therefrom will be pledged to the holders of the Bonds, usually DASNY on behalf of the library and a holder of the Bonds should not regard the mortgage as security for payment of principal of and interest on those Bonds. Property subject to the mortgage may be released and the Mortgage may be amended without the consent of the Trustee Bank or the holder of any of the Bonds.

Events of Default and Acceleration of the Library Loan

In a DASNY library transaction, the DASNY Resolution usually provides for what happens in the event of a default by the library or DASNY in the payment of amounts due to the DASNY bondholders. The following are typical events of default under the DASNY Resolution: (i) a default in the payment of the principal, or redemption price of or interest on such Bonds; (ii) the Authority takes any action, or fails to take any action, which would cause such Bonds to be “arbitrage bonds” within the meaning of the Code, or fails to comply with the provisions of the Code and as a result thereof, interest on Library Bonds becomes includable in gross income for federal income tax purposes; (iii) a default by the Authority in the due and punctual performance of any other covenant, condition, agreement or provision contained in the Bonds or in the DASNY Resolution which continues for 30 days after written notice thereof is given to the Authority by the Trustee Bank (such notice to be given at the Trustee’s discretion or at the written request of holders of not less than 25% in principal amount of outstanding bonds); or (iv) an “Event of Default,” as defined in the Loan Agreement arising out of or resulting from the failure of the Library to comply with the Loan Agreement, has occurred and is continuing and all sums payable by the Library under the Loan Agreement have been declared immediately due and payable (unless such declaration has been annulled). (Unless all sums payable by the Library under the Loan Agreement are declared immediately due and payable, an event of default under the Loan Agreement is not an event of default under the DASNY Resolution.)

The Resolution may typically provide that if an event of default (other than as described in clause (ii) of the preceding paragraph) occurs and continues, the Trustee Bank must, upon the written request of the holders of not less than 25% in principal amount of the outstanding bonds, declare the principal of and interest on all the outstanding bonds to be due and payable immediately. At the expiration of 30 days from the giving of such notice, such principal and interest shall become immediately due and payable.

The Trustee Bank may, with the written consent of the holders of not less than 25% in principal amount of the Bonds then outstanding, annul such declaration and its consequences under the terms and conditions specified in the DASNY Resolution with respect to such annulment.

Upon the happening and continuance of any event of default, the Trustee Bank may proceed, and upon the written request of the holders of not less than twenty-five per centum (25%) in principal amount of the outstanding bonds of a series, shall proceed to protect and enforce its rights and the rights of the holders by such suits, actions or special proceedings in equity or at law for the performance of any covenant contained in the DASNY Resolution.

The DASNY Resolution may typically provide that the Trustee Bank shall give notice in accordance with the Resolution of each event of default known to the Trustee Bank to the holders of the bonds within 30 days, after knowledge of the occurrence thereof unless such default has been remedied or cured before the giving of such notice; provided, however, that except in the case of default in the payment of principal or redemption price of, or interest on, any of the Bonds, the Trustee Bank shall be protected in withholding such notice thereof to the Holders if the Trustee in good faith determines that the withholding of such notice is in the best interests of the holders of the DASNY Bonds.

It is good that you read these typical provisions on events of default and subsequent acceleration of loan terms, but it is exceeding unlikely that a library would ever find itself in this situation.

State Not Liable On Library Bonds Issued By DASNY To Benefit Public Libraries

The Act provides that notes and bonds of the Authority shall not be a debt of the State nor shall the State be liable thereon, nor shall such notes or bonds be payable out of any funds other than those of the Authority. The Resolution adopted by the DASNY Board in connection with a financing for your library would specifically provide that the Bonds issued for your behalf, shall not be a debt of the State nor shall the State be liable thereon.

Covenant By The State to holders of DASNY Bonds

The Act states that the State pledges and agrees with the holders of the Authority's notes and bonds that the State will not limit or alter the rights vested in the Authority to provide projects, to establish and collect revenues therefrom and to fulfill agreements with the holders of the Authority's notes and bonds or in any way impair the rights and remedies of the holders of such notes or bonds until such notes or bonds and interest thereon and all costs and expenses in connection with any action or proceeding by or on behalf of the holders of such notes or bonds are fully met and discharged. Notwithstanding the State's pledges and agreements contained in the Act, the State may in the exercise of its sovereign power enact or amend its laws which, if determined to be both reasonable and necessary to serve an important public purpose, could have the effect of impairing these pledges and agreements with the Authority and with the holders of the Authority's notes or bonds.

Steps In A "Dorm" Library Bond Issue

1. If you are a free association library, check the establishment proceedings and other documentation and the current by-laws for provisions on debt.
2. Check your basic documentation file for your federal tax status. Are you a Section 501(c)(3) organization? Are you a special legislation district? Do you have a current contract with your Affiliated Entity (if required)?
3. Hire competent Bond Counsel and get legislation drafted and adopted adding your library to list of entities for which Dorm can finance projects. (Please note the word "competent.")
4. Ask the Secretary of State or Board of Regents, as applicable for a "bring-down" type certificate so you are sure of your current existent status.
5. In certain cases, adopt a resolution requesting the local political subdivision which is your Affiliated Entity to hold a public hearing on your behalf and with your participation.
6. In certain cases, hold a public hearing in conjunction with your local political subdivision on at least 14 days published notice. The notice must include: (a) a functional description of the project, including street address of building or location for equipment, (b) maximum estimated cost, (c) sources of funding, including amount of debt, and (d) the owner/operator of the project.

7. Adopt a resolution requesting the Affiliated Entity to hold a public referendum on an increase to the annual funding of the public library district or free association library district sufficient to cover maximum anticipated debt service on any bonds issued for the capital project after discussion with the Dorm about interest rates. (If you find anyone who can accurately predict interest rates in the future, please call us on our personal cell phones. We want to be their friend.)
8. In certain cases, obtain either a resolution of that political subdivision's legislative body or a certificate of their chief executive officer approving the issuance of the particular maximum amount of debt for the particular purpose, as described in the public hearing notice. Alternatively, the public vote may suffice for this purpose.
9. Adopt a resolution of your board of trustees by a simple majority vote to: (a) authorize the issuance of debt obligations in the particular maximum amount and for the particular purpose, (b) authorize the Chairperson and Treasurer of the association to sign necessary documentation to sell such debt, and (c) approve any needed security agreement such as a mortgage.
10. Begin discussions with Dorm on a timetable for debt issuance. DASNY adopts necessary resolutions and then drafts loan agreement and other loan documentation, and obtain requisite State approval.
11. Dorm sells bonds for your library, closes the transaction, and gives you the funds.
12. Build new library additions; buy new mobile library truck.
13. Celebrate.

And, oh, yes, remember to budget to repay the loan on time. Please.

CHAPTER TWENTY-TWO

Types of "Public" Libraries and Their Financing Options—Summary Overview

Having gone into some detail on library financings, particularly those for public libraries affiliated with school districts, let us now stop and catch our breath with a summary overview of the rules for each type "public library."

The Library District Affiliated With A School District

- Elected Board of Trustees.
- Authorized to submit budget to voters and request an increase in the library district tax including for a capital project (including in small city school districts since Chapter 171 of the Laws of 1996).
- Not authorized to issue general obligation type debt. Not authorized to itself pledge school district credit.
- Authorized to enter into conventional purchase money mortgage note.
- Must rely on Affiliated School District to issue general obligation bonds and notes with the School District pledge of its own credit.

The Public Library District Established By Special Legislation

- A Library District similar to those affiliated with a school district.
- Can be authorized in a town, village, county and/or city only by special legislation.
- Any authorization to levy a tax and/or any authorization to issue general obligation indebtedness (by the District or an Affiliated Entity or Entities) must be spelled out in the particular legislation. May include specific authority to issue debt through the Dormitory Authority.

The Municipal Public Library (Department or Branch of Municipality)

- Board is appointed by municipality.
- Neither authorized to levy a tax nor to issue indebtedness of any variety.

- Budget subject to Affiliated Entity/municipal legislative action but may be increased by vote of the people in the municipality in certain cases on petition pursuant to Chapter 414 of the laws of 1995.
- Any financing for a library purpose must follow the general rules applicable to the town, village, city or county, which can issue such general obligation debt if library is a department of that political subdivision.
- A separate municipality can contract with a municipal library in another political subdivision but it cannot bond to help it.

The Free Association Library (No District)

- Not authorized to levy a tax. Can receive support by contract for services with a municipality or school district but no political subdivision may issue debt for them.
- A private organization, not a governmental agency nor a political subdivision.
- Not authorized to issue general obligation type debt.
- No political subdivision may issue debt for them.
- Authorized to enter into conventional purchase money mortgage note and can be authorized to do bond financing with local Industrial Development Agency or the Dormitory Authority.

The Free Association Library District And Its Municipal/School District Affiliated Entity

- Not authorized to levy a tax directly.
- Budget subject to municipal legislative action but can be increased by vote of the people in the municipality, should the municipal/school district board not chose on their own pursuant to Chapter 414 of the Laws of 1995.
- Can receive support from an Affiliated municipal or school district and have support increased by vote of that entity or directly by municipality voters on petition of 10% of voters (Chapter 414, Laws of 1995).
- No political subdivision may issue debt for them.
- Authorized to enter into conventional purchase money mortgage note and can be authorized to do bond financing with local Industrial Development Agency or the Dormitory Authority.

A “City and County Library”

- A specially chartered entity with its own rules pursuant to Chapter 768 of the Laws of 1953. Established by a county legislative body with a board of trustees appointed by same.
- A separate and distinct public corporation, not a branch of county government.
- Nevertheless, dependent on the county for its budget and to “provide buildings and accommodations therefore.”

- Chapter 768 specifically authorizes such a library to mortgage property and provides such a library with "all of the powers and duties of other educational institutions of the University of the State of New York" and "exclusive powers and duties" to "generally do, perform and carry out all the necessary, usual or customary acts and duties required by law and done and performed by trustees of libraries in the State of New York."
- Without authority to issue Local Finance Law "general obligation" debt, but the county may do so for library projects with standard bond authorization procedures.

Joint Public Libraries

- A public library with more than one Affiliated Entity is usually the creation of a special act of the State Legislature. That legislation must be reviewed for the requirements for a capital improvement project.
- In any case in which a public library has more than one Affiliated Entity and no special legislation, it is likely the result of a long-term contractual agreement between two political subdivisions (town, cities, counties, villages, school districts) and that contract should be consulted for the allocation and treatment of capital project financings.

APPENDIX A

Transactional Players and their Roles

Beneficial Bond Holder/Owner:	The actual person, pension fund, corporation or mutual fund who owns the note or bond.
Bond Counsel:	Provides validity and tax opinion on school district or municipal debt or an IDA or Dormitory Authority financing for the benefit of the buyer. Drafts bond related proceedings including library referendum proceedings and sale and closing documentation.
Bond Insurer:	A company that promises to pay debt service on debt it insures if the issuer does not. Sometimes purchased by winning bidders in competitive bond sales or can be part of a negotiated transaction.
Bureau of Public Debt:	Division of the U.S. Treasury Department that issues debt to school districts and municipalities for advance refunding escrows.
Chief Fiscal Officer:	The Board President of a School District, Village Treasurer, City Treasurer or Comptroller, Town Supervisor, County Treasurer and for you, your Library District Treasurer.
DASNY:	The Dormitory Authority of the State of New York.
DTC:	The Depository Trust Company, a corporation formed by banks and investment banks to act as a depository and serve a central processing function for debt sold in book-entry only (i.e. electronic form without each holder getting its own physical paper bonds or note certificate; ownership recorded electronically).

Escrow Agent/Holder:	Bank located and authorized to do business in the State, and acting as holder of U.S. Treasury securities in escrow for refunded bond debt service.
Financial Advisor:	Consultant to Library District and Affiliated Entity on financings, structuring bond and note issues and related matters, including preparation of Official Statements and disclosure law annual compliance of materials.
Fiscal Agent:	Often same as paying agent. Keeps record of owners of a bond or note issue and conversions if needed. The officer named in LFL to this role can delegate to an authorized bank.
General Obligations:	The only type of debt a municipality or school district may issue in New York State, pledging the faith and credit and unlimited taxing power of the municipality or school district.
Investment Banker:	A person employed by an underwriter to develop negotiated transactions in notes or bonds with municipalities, and school districts usually an officer of an investment bank or a regular bank.
Issuer:	The local political subdivision or school district, not the library district itself (except in the case of a mortgage note).
Letter of Credit Bank:	Sometimes used in the note market (like bond insurance).
Library District:	As used herein, a public library typically affiliated with a school district, with the power to levy taxes for its operations and to put forward propositions for capital improvements.
Local Counsel:	Library District Attorney.
National Repository:	Filing locale for updated material information about an issuer. Municipal Securities Rulemaking Board since July 1, 2009

Objects or Purposes: Legal term for a capital project or capital items.

Paying Agent: Who pays debt service to the holder (or DTC) as and when due.

Rating Agencies: Independent companies which rate bonds and notes, such as Moody's, Standard & Poor's and Fitch Ratings.

Rebate Compliance Provider: Vendor, usually the financial advisor that helps an issuer determine its arbitrage rebate liability, if any.

State Comptroller: You know what these people do (oversees all the financial aspects of the local government).

Taxpayer: You know who these people are (Ws—working citizens and residents, including Gus. You know Gus. Every Board has one. He sits in the back of the room and doesn't like anything you do. If he had as much money as time, you'd be in court constantly.)

Trustee Bank: *See* Escrow Agent, Paying Agent, Fiscal Agent: A bank or trust company located and licensed to do business in the State, with trust powers to hold and distribute bond proceeds.

Underwriter: A bank or investment bank which is a "broker dealer" buying municipal debt for resale.

Underwriter's Counsel: Lawyers for the buyers in a negotiated transaction.

Verification Agent: An independent specialized accounting firm which verifies that money deposited in the escrow account in an advance refunding is sufficient to pay the intended principal and interest on refunded debt.

APPENDIX B

Sample Bond Counsel Opinion of General Obligation Debt

September 27, 2009

Duke Central School District,
Earl County,
State of New York

Re: Duke Central School District, Earl County, New York
$4,155,000 Library Improvement (Serial) Bonds, 2009

Ladies and Gentlemen:

We have been requested to render our opinion as to the validity of an issue of $4,155,000 Library Improvement (Serial) Bonds, 2009 (the "Obligations"), of the Duke Central School District, Earl County, State of New York (the "Obligor"), dated September 15, 2009, initially issued in registered form in denominations such that one bond shall be issued for each maturity of bonds in such amounts as hereinafter set forth, bearing interest at the rate of three and eighty-five hundredths per centum (3.85%) per annum, payable on March 15, 2010 and semiannually thereafter on September 15 and March 15, and maturing in the amount of $225,000 on September 15, 2010, $230,000 on September 15, 2011, $250,000 on September 15, 2012, $275,000 on September 15 in each of the years 2013 to 2018, both inclusive, and $300,000 on September 15 in each of the years 2019 to 2024, both inclusive. **[Description of the debt obligation].**

Bonds maturing on or before September 15, 2018 are not subject to redemption prior to maturity. Bonds maturing on or after September 15, 2019 are subject to redemption prior to maturity as a whole or in part (and by lot if less than all of a maturity is to be redeemed) at the option of the School District on September 15, 2018 or on any interest payment date thereafter at par, plus accrued interest to the date of redemption. **[Description of the early redemption features, if any].**

We have examined:

(1) the Constitution and statutes of the State of New York;

(2) the Internal Revenue Code of 1986, including particularly Sections 103 and 141 and 150 thereof, and the applicable regulations of the United States Treasury Department promulgated thereunder (collectively, the "Code");

(3) an arbitrage certificate executed on behalf of the Obligor which includes, among other things, covenants, relating to compliance with the Code, with the owners of the Obligations that the Obligor will, among other things, (i) take all actions on its part necessary to cause interest on the Obligations not to be includable in the gross income of the owners thereof for Federal income tax purposes, including, without limitation, restricting, to the extent necessary, the yield on investments made with the proceeds of the Obligations and investment earnings thereon, making required payments to the Federal Government, if any, and maintaining books and records in a specified manner, where appropriate, and (ii) refrain from taking any action which would cause interest on the Obligations to be includable in the gross income of the owners thereof for Federal income tax purposes, including, without limitation, refraining from spending the proceeds of the Obligations and investment earnings thereon on certain specified purposes; and

(4) a certificate executed on behalf of the Obligor which includes, among other things, a statement that compliance with such covenants is not prohibited by, or violative of, any provision of local or special law, regulation or resolution applicable to the Obligor.

We also have examined a certified copy of proceedings of the finance board of the Obligor and other proofs authorizing and relating to the issuance of the Obligations, including the form of the Obligations. In rendering the opinions expressed herein we have assumed the accuracy and truthfulness of all public records, documents and proceedings, including factual information, expectations and statements contained therein, examined by us which have been executed or certified by public officials acting within the scope of their official capacities, and have not verified the accuracy or truthfulness thereof. We also have assumed the genuineness of the signatures appearing upon such public records, documents and proceedings and the certifications thereof. **[Description of the law and documentation reviewed].**

In our opinion:

(a) The Obligations have been authorized and issued in accordance with the Constitution and statutes of the State of New York and constitute valid and legally binding general obligations of the Obligor, all the taxable real property within which is subject to the levy of ad valorem taxes to pay the Obligations and interest thereon, without limitation as to rate or amount; provided, however, that the enforceability (but not the validity) of the Obligations (i) may be limited by any applicable bankruptcy, insolvency or other law now existing or hereafter enacted by said State or the Federal government affecting the enforcement of creditors' rights, and (ii) may be subject to the exercise of judicial discretion in appropriate cases. **[Validity Opinion].**

(b) The Obligor has the power to comply with its covenants with respect to compliance with the Code as such covenants relate to the Obligations; provided, however, that the enforceability (but not the validity) of such covenants may be limited by any applicable bankruptcy, insolvency or other law now existing or hereafter enacted by said State or the Federal government affecting the enforcement of creditors' rights. **[Covenant authority of the issuer].**

(c) Interest on the Obligations is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, and is exempt from personal income taxes imposed by the State of New York and any political subdivision thereof (including The City of New York). Interest on the Obligations is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, not is it included in adjusted current earnings in calculating corporate alternative minimum taxable income. We express no opinion regarding other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Obligations. **[Federal Tax Status Opinion]**

Certain agreements, requirements and procedures contained or referred to in the Arbitrage Certificate and other relevant documents may be changed and certain actions (including, without limitation, economic defeasance of the Obligations) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. **[Qualifications].**

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. Accordingly, this opinion is not intended to, and may not, be relied upon in connection with any such actions, events or matters. Our engagement with respect to the Obligations has concluded with their issuance, and we disclaim any obligation to update this opinion. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents. Furthermore, we have assumed compliance with all covenants and agreements contained in the Arbitrage Certificate, including without limitation covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Obligations to be included in gross income for federal income tax purposes or no longer exempt for purposes of personal income taxes imposed by the State of New York or any political subdivision thereof (including The City of New York). We call attention to the fact that the rights and obligations under the Obligations and the Arbitrage Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium or other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against municipal corporations such as the Obligor in the State of New York. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum, choice of venue, or waiver provisions contained in the foregoing documents. **[Assumptions underlying the opinion].**

The scope of our engagement in relation to the issuance of the Obligations has extended solely to the examination of the facts and law incident to rendering the opinions expressed herein. Such opinions are not intended and should not be construed to express or imply any conclusion that the amount of real property subject to taxation within the boundaries of the Obligor, together with other legally available sources of revenue, if any, will be sufficient to enable the Obligor to pay the principal of or interest on the Obligations as the same respectively become due and payable. Reference should be made to the Official Statement prepared by the Obligor in relation to the Obligations for factual information which, in the judgment of the Obligor, could materially affect the ability of the Obligor to pay such principal and interest. While we have participated in the preparation of such Official Statement, we have not verified the accuracy, completeness or fairness of the factual information contained therein and, accordingly, we express no opinion as to whether the Obligor, in connection with the sale of the Obligations, has made any untrue statement of a material fact or omitted to state a material fact necessary in order to make any statements made, in the light of the circumstances under which they were made, not misleading. **[What the opinion does not cover].**

Very truly yours,

APPENDIX C

Library District Improvement Program Time Line

1. **SEQRA Determination:**
   SEQRA is an acronym for State Environmental Quality Review Act. This law was enacted to ensure that any capital project will not have a significant adverse impact upon the environment. Every District capital project should be in compliance with SEQRA before the Board adopts any proceeding to undertake the capital project, including a resolution calling a bond referendum.

   Pursuant to legal and regulatory changes affecting the SEQRA process for school districts, since September 1,2001, S.E.D. is no longer automatically the Lead Agency for public school construction projects—the question of compliance with SEQRA is now the responsibility of the Board of Education as Lead Agency, generally.

   The conduct of the SEQRA process is usually within the scope of duties of your local counsel. Bond Counsel, of course, can be available to assist in this regard.

   Time Parameters: Consult your general counsel and the project architect—the time parameters are difficult to gauge as it can differ from project to project depending upon what “type” of “action” the project is under SEQRA. It is a relative “slam dunk” for a type II action, suggesting the mere determination that the project constitutes a type II action, thus requiring no further determinations; for an uncomplicated unlisted action the process can take approximately 30 to 60 days, if more complicated, the process could approach the length of time for a type I action; a type I action could take as long as 4 months or more if a full environmental assessment form or draft environmental impact statement is required. This is the largest procedural hurdle in the capital construction process - this should be done before the school district commits to a referendum date for your Library District project.

2. **Fax *and* send each evidence of SEQRA compliance** (generally this will be the negative declaration) to bond counsel.

3. **School Board of Education adopts resolution providing for submission of bond proposition for the Library District at a special or the annual district meeting/election.** (3/5 affirmative vote).

4. **Publish notice of referendum 45 days in advance of referendum date** in 2 newspapers having general circulation in School District—*allow* 8 weeks.

5. **After successful vote, School District Board of Education must adopt bond resolution by two-thirds affirmative vote to implement vote of the people**—*allow* 1-2 weeks.

6. **After adoption of bond resolution, publish Legal Notice of estoppel in official newspaper(s) of School District**—*allow* 1 week from date of adoption to date of publication. (Ignore this for city school district—see above.)

7. **After 20 days has expired from publication of Legal Notice of estoppel**, School District is in a position to issue obligations subject to any Education Department approval—*allow* 3 weeks.

8. **District receives final approval of plans and specifications** from Commissioner of Education (if required). Some planning costs may be borrowed prior thereto.

9. **After final approval, must advertise for project bids**—at least 5 days must elapse between first publication of advertisement and the date specified for opening and reading of bids. Counting architect's time to prepare the bids *allow* at least a month for the whole process —consult architect.

10. **To sell bond anticipation notes or serial bonds with an official statement** *allow* minimum of 4 weeks to 6 weeks—consult financial advisor.

11. ***Allow* seven days minimum from sale of notes to delivery of notes;** ten to fourteen days for serial bonds (from sale to delivery).

The Entire process, on average, could take 7 to 16 months from start to finish, not counting time spent by the Library Board of Trustees in the planning stage.

About the Authors

Douglas E. Goodfriend, a New York Public Finance partner, has extensive experience in municipal general obligation financings for various New York counties, cities, towns, villages, school districts, and fire districts. He frequently serves as bond counsel to municipal and school district issuers participating in the financing programs of the New York State Environmental Facilities Corporation and the Dormitory Authority of the State of New York, and the grant and loan programs of the Rural Development division of the United States Department of Agriculture.

Mr. Goodfriend's specialized areas of New York municipal law interest include open spaces programs and financings, town and county improvement district formation, consolidation and improvement, innovative lease-purchase financings, school district bond resolution referendum law, library projects, village local improvement programs and the drafting of local laws and propositions, as well as state legislation on behalf of clients.

Mr. Goodfriend is a frequent speaker at professional municipal organizations on local finance law, federal securities law, and federal tax matters affecting municipal debt issuance. You can contact him at 1-212-506-5211 or dgoodfriend@orrick.com.

Thomas E. Myers, a New York Public Finance partner, has extensive experience in financings for various New York municipalities, school districts, and fire districts in connection with over $6 billion in general obligation financings. Mr. Myers' practice also focuses on financings for industrial development bonds, local development corporations, housing bonds, resource recovery and water/sewer authority revenue bonds. Mr. Myers has extensive experience as underwriter's and placement agent's counsel on a wide variety of public finance matters. In addition, Mr. Myers was special counsel in connection with tax lien and tobacco settlement securitizations by various New York counties. Mr. Myers was named Dealmaker of the

Year by *The American Lawyer* in 2001 for his innovative work on the first pooled counties tobacco securitization. He is a graduate of Marquette University and the Syracuse College of Law, past chair of the Municipal Law Section of the New York State Bar Association and a frequent speaker at meetings of various municipal organizations. You can contact him at 1-212-506-5212 or tmyers@orrick.com.

Mr. Myers and Mr. Goodfriend are the authors of the Bond Basics series of primers for counties, cities, towns, villages and fire districts, as well as school districts and library districts in New York State, which distill their combined 50 years of public finance legal experience. Mr. Myers and Mr. Goodfriend may also be reached at their toll-free number, 1-800-295-8506.

ABOUT ORRICK

Orrick, Herrington & Sutcliffe LLP has maintained a substantial law practice in the area of public finance for nearly a century. Our lawyers provide bond counsel services to libraries throughout New York State and are committed to providing cost-effective and innovative services and solutions for all types of public finance matters.

For additional information about our practice in New York State, please contact us at **publicfinance@orrick.com**, visit our website at **www.orrick.com** or call us at 800-295-8506.

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