



PECK, SHAFFER & WILLIAMS LLP
ATTORNEYS AT LAW
65 EAST STATE STREET, SUITE 500
COLUMBUS, OH 43215

TEL 614 224 5205
888 900 5205
FAX 614 224 0069
WWW.PECKSHAFFER.COM

MEMORANDUM TO CLIENTS

OHIO BOND ISSUE ELECTION PROCEDURE

From time to time, an Ohio political subdivision, such as a township, municipal corporation (city or village), school district or county, may find it advisable to issue voted general obligation bonds to finance public improvements. The procedure for placing such a voted bond issue on the ballot is set out in Chapter 133 (the “Uniform Public Securities Law” or the “Act”) of the Ohio Revised Code (the “ORC”), and this memorandum will address some general questions regarding that election procedure.

What improvements may be financed with voted general obligation bonds?

Voted general obligation bonds may be issued for the purpose of paying all or any portion of the costs of any “permanent improvement” that the subdivision is authorized, alone or in cooperation with other persons, to acquire, improve, or construct. (ORC 133.15(A)) A “permanent improvement” is any property, asset, or improvement certified by the fiscal officer of the subdivision as having an estimated life or period of usefulness of five years or more. (ORC 133.01(CC))

How long may improvements be financed?

The maximum amount of time over which various classes of improvements may be financed with general obligations bonds is set out in ORC 133.20, and ranges from five to 50 years, based generally upon the Ohio General Assembly’s view of the hypothetical useful life of those improvements. For example, water and sewer utility improvements may be financed for up to 40 years, while new motor vehicles (such as police cruisers) may be financed for up to five years.

If a single project is comprised of more than one category of improvements set out in ORC 133.20, the subdivision’s fiscal officer must calculate a weighted average of the improvements comprising the project, which weighted average becomes the maximum maturity for the bond issue. (ORC 133.20(E)) In the case of a class of improvements not listed (such as buildings), the maximum maturity is the fiscal officer’s estimate of the life or period of usefulness of the improvements but in any case, not greater than 30 years. (ORC 133.20(C))

While the Act establishes the maximum amount of time improvements may be financed, the taxing authority may issue bonds for a lesser period of time. This often occurs when, for example, prudent financial management requires that the debt incurred for a given asset not last longer than the actual useful life of that asset, or when the municipal bond market will not accept bonds beyond a given maturity.

What is the procedure for placing the question of issuing general obligation bonds on the ballot?

The steps in placing a bond issue on the ballot are as follows:

1. The taxing authority of the subdivision determines the improvements to be included in the bond issue. The bond issue must be confined to “one purpose”, as defined for purposes of the Act. (ORC 133.18(A))
2. The fiscal officer of the subdivision determines the maximum permitted maturity of the proposed bond issue by applying statutory maximum maturities for the various classes of improvements to be included in the bond issue, as described above, and certifies that maximum maturity to the taxing authority of the subdivision. (ORC 133.19 and .20)
3. The taxing authority of the subdivision passes legislation (an ordinance or resolution) that does all of the following:
 - (a) Declares the necessity and purpose of the bond issue;
 - (b) States the date of the election at which the question shall be submitted to the electors of the subdivision;
 - (c) States the following terms of the proposed bond issue:
 - (i) principal amount,
 - (ii) approximate date,
 - (iii) estimated “net average” rate of interest, and
 - (iv) maximum number of years over which the principal of the bonds may be paid, which may not exceed the maximum maturity determined by the fiscal officer in the certificate described in 2. above. (ORC 133.18(B)); and
 - (d) Declares the necessity of levying a tax outside the tax limitation to pay the debt charges on the bonds and any notes issued in anticipation of the bonds. (ORC 133.18(B)).
4. The taxing authority certifies a copy of the legislation described in 3. above to the county auditor. (ORC 133.18(C))
5. The county auditor calculates and certifies to the taxing authority the estimated average annual property tax levy, expressed in cents or dollars and cents for each one hundred dollars of tax valuation and in mills for each one dollar of tax valuation, that the county auditor estimates to be required throughout the stated maturity of the bonds to pay the debt charges on the bonds. (ORC 133.18(C))

6. After receiving the county auditor's calculation described in 5. above, the taxing authority determines to proceed with submitting the question of the issue of securities to the electors by passing legislation to that effect. (ORC 133.18(D))
7. The taxing authority files the following items with the board of elections not later than 90 days prior to the date of the election:
 - (a) Copies of the legislation described in 3. and 6. above, and
 - (b) A copy of the county auditor's certification described in 5. above. (ORC 133.18(D))

An updated listing of the election deadlines may be accessed on our website:

<http://www.peckshaffer.com/>

under the drop-down menu "News and Events".

or

We would be pleased to discuss the applicable 90-day deadline once an election date has been determined.

8. The board of elections publishes a notice of the election, in one or more newspapers of general circulation in the subdivision, at least once no later than ten days prior to the election. (ORC 133.18(E)(3))
9. The board of elections conducts the election on the designated date using statutorily prescribed ballot language and certifies the results of the election to the State Tax Commissioner, the county auditor and the fiscal officer of the subdivision. (ORC 133.18(E), (F) and (G))
10. If a majority of the electors voting upon the question vote for it, the taxing authority of the subdivision may proceed to issue bonds under ORC 133.23 or notes in anticipation of bonds pursuant to ORC 133.22, and levy and collect a property tax outside the "ten-mill" tax limitation during the period the securities are outstanding sufficient in amount to pay the debt charges on the securities, including debt charges on any anticipatory securities required to be paid from that tax. (ORC 133.18(H))

How should the taxing authority determine the estimated "net average" interest rate required for the legislation described in 3.(c) above?

Since the bonds will not be marketed to investors - and thus, the actual interest rate on the bonds known - until after the election, the determination of the estimated "net average" interest rate used to place the issue on the ballot is a political decision of the taxing authority.

The last paragraph of ORC 133.18(B) says that the “net average” interest rate is determined by the taxing authority based on, among other factors, then existing market conditions, and may reflect adjustments for any anticipated direct payments expected to be received by the taxing authority from the federal government relating to the bonds and the effect of any federal tax credits anticipated to be available to owners of all or a portion of the bonds.

By law, the bonds, when sold after a successful election, will bear interest at whatever the interest rate is at the time of sale, even if that rate is in excess of the estimated rate set forth in the pre-election proceedings. (ORC 133.18(B), last paragraph) Politically, however, the taxing authority should expect an adverse reaction from the voters and taxpayers should the amount of taxes actually billed exceed the estimate set forth in the ballot.

Consequently, in making its determination, a taxing authority should seek advice about the estimated net average interest rate from persons knowledgeable in municipal finance. Out of conservatism, many taxing authorities add a “safety margin” to the current interest rate because of the unpredictability of future interest rates for municipal bonds. A taxing authority must balance against such conservatism the reality that, if all other factors remain constant, the higher the estimated net average interest rate, the higher the estimated millage that will appear on the ballot and consequently, the less likely it is that the voters will approve the issue.

How is the principal amount of the proposed bond issue determined since the cost of the improvements will not be known until after the election? May additional bonds be issued if the cost is higher than expected?

As with the estimated net average interest rate, the setting of the principal amount of a proposed bond issue is a political determination by the taxing authority. By law, the principal amount of securities issued after a successful election may not exceed the principal amount shown on the ballot, even though the cost of the project as described exceeds good-faith pre-election estimates. While this would argue in favor of inflating the principal amount to cover any possible contingency, there is a counter-consideration which is that, if all other factors remain constant, the larger the principal amount, the higher the estimated millage that will appear on the ballot and consequently, the less likely it is that the voters will approve the bond issue.

The taxing authority should assure that adequate contingency amounts are included in project cost estimates used in making its determination to provide a “cushion” against possible variances in the actual cost of the financed improvements. Also, experienced architects and engineers are able to design many projects with options that may be included or deleted depending upon the final costs of the improvements.

The principal amount on the ballot is a maximum permitted amount, and the taxing authority may issue a lesser amount of bonds should the actual cost of the proposed improvements be less than expected.

With the various bond issue structures now permitted and changes in our assessed valuation, how does the county auditor calculate the estimated annual tax levy needed to pay debt service on the proposed bond issue?

In calculating the estimated average annual property tax levy, the county auditor is required to assume that:

- (1) The bonds are issued in one series bearing interest and maturing in substantially equal principal amounts in each year over the maximum number of years over which the principal of the bonds may be paid as stated in the taxing authority's legislation, and
- (2) The amount of the tax valuation of the subdivision for the current year remains the same throughout the maturity of the bonds. If the tax valuation for the current year is not determined, the county auditor must base the calculation on the estimated amount of the tax valuation submitted by the county auditor to the county budget commission.

We expect that our bond issue will vary from the formula used by the county auditor in ways that will make it more attractive to the voters. May the ballot language incorporate those expected variances?

It is not uncommon for the actual bond issue anticipated by a taxing authority to differ from the bond issue described by the statutory county auditor's formula. For example, instead of level annual principal payments, it may be expected that the bonds will have level annual payments of principal and interest. Or, instead of a single interest rate, the bonds may be expected to have a different interest rate for different maturities. Or, it may be expected that the subdivision's assessed valuation will be higher in subsequent years, thereby reducing the needed bond millage in those years.

Regardless of any such expected variances, the county auditor's calculation must follow the statutory formula, and the ballot language must follow the wording prescribed by statute, even though those variances may make a proposed bond issue more acceptable to the voters. While any such variances may not be incorporated into the bond election proceedings, they may be made part of informational materials developed for the bond issue campaign.

May the purpose clause of the proposed bond issue be "enhanced" so as to make the bond issue more compelling to the voters?

A taxing authority may wish to describe the purpose of a proposed bond issue in a way that will make voters more likely to approve the issue, for example by elaborating on the merits of the proposed improvements. Legally, the purpose clause must be straightforward and factual, and may not be argumentative. While each case depends on its facts and context, the local board

of elections or the Ohio Secretary of State may be expected to reject bond issue language that violates this standard.

Is there any limit on the amount of voted general obligation debt that may be issued?

There is no single limitation on voted general obligation debt applicable to all Ohio political subdivisions. The Act does contain limits on voted debt applicable to specific types of subdivisions based upon the concept of “net indebtedness”, as defined in ORC 133.04. The limitation generally applicable to municipalities is set out in ORC 133.05, to school districts in ORC 133.06, to counties in ORC 133.07, and to townships in ORC 133.09.

Also, particular provisions in the Ohio Revised Code may limit the amount of voted general obligation debt that may be issued. For example, ORC 505.40 limits the amount of voted bonds issued by a township for providing fire apparatus and appliances, buildings or sites therefor, sources of water supply and materials therefor, or for the establishment and maintenance of lines of fire-alarm telegraph, to a maximum of the greater of (a) one hundred fifty thousand dollars or (b) two per cent of the total value of all property in the township as listed and assessed for taxation.

We have sufficient revenues to support a new bond issue, but because of unvoted debt limits, we need to have the bonds approved by the voters. Is the ballot language concerning property taxes required if it is not expected to be needed for debt service?

Under the Act, a bond issue election is, in fact, a single referendum on two different questions:

- (1) Shall the subdivision, as a matter of public policy, incur debt for the specified public improvements?
- and
- (2) Shall an ad valorem property tax be imposed to pay the debt service on that indebtedness?

Once a bond issue is approved by the voters, if the revenues from the property tax approved as part of the bond issue are not required to pay debt service in a particular year (for example, because some other source of revenues - such as municipal income tax revenues or county sales tax revenues - will be available and used to pay the bond debt service), the property tax need not be levied by the taxing authority for that year.

Even though it may be expected that some source of revenues other than property taxes will be available and used to pay some or all the debt service on the proposed bonds, the Act requires the inclusion of the property tax question on the ballot. The informational materials developed for the bond issue campaign may, of course, educate voters as to the expected source of payment of the debt, and that some or all of the property tax is not expected to be levied.

Conclusion

Ohio law and the Act provide elaboration on the application of many of the matters discussed in this memorandum to particular circumstances. While this memorandum is general in nature, we hope that its information will be useful in developing any voted bond issues that may be under consideration.

We would be pleased to discuss this memorandum or other matters related to proposed bond or note issues. Contact information for our Cincinnati and Columbus, Ohio offices and the attorneys in those offices is located on the World-Wide Web at:

<http://www.peckshaffer.com/>

under the heading “Offices”.

PECK, SHAFFER & WILLIAMS LLP

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