

Municipal Budgets and Finance

21st Annual Riley Fletcher Basic Municipal Law Seminar
Austin, Texas
Friday, February 9, 2024

Kuruvilla (K.O.) Oommen
City Attorney
City of Irving, Texas

Overview

1. Municipal Budgets & Tax Rate
2. Public Purpose Doctrine
3. Municipal Borrowing
4. Municipal Depositories
5. Municipal Investments

Resources

- ***Handbook for Mayors and Councilmembers (2022)***
<https://www.tml.org/DocumentCenter/View/1289/HandbookforMayorsandCouncilmembers?bidId=>
- ***TML Revenue Manual for Texas Cities (Nov. 2023)***
<https://www.tml.org/DocumentCenter/View/3989/Revenue-Manual-November-2023>
- ***Texas Municipal Law and Procedure Manual (2022, 7th edition)***
<https://tmca.memberclicks.net/texas-municipal-law-procedure-manual>
- ***Municipal Budget & Finance Paper***

Municipal Budgets and Tax Rates

- **Statutes:**

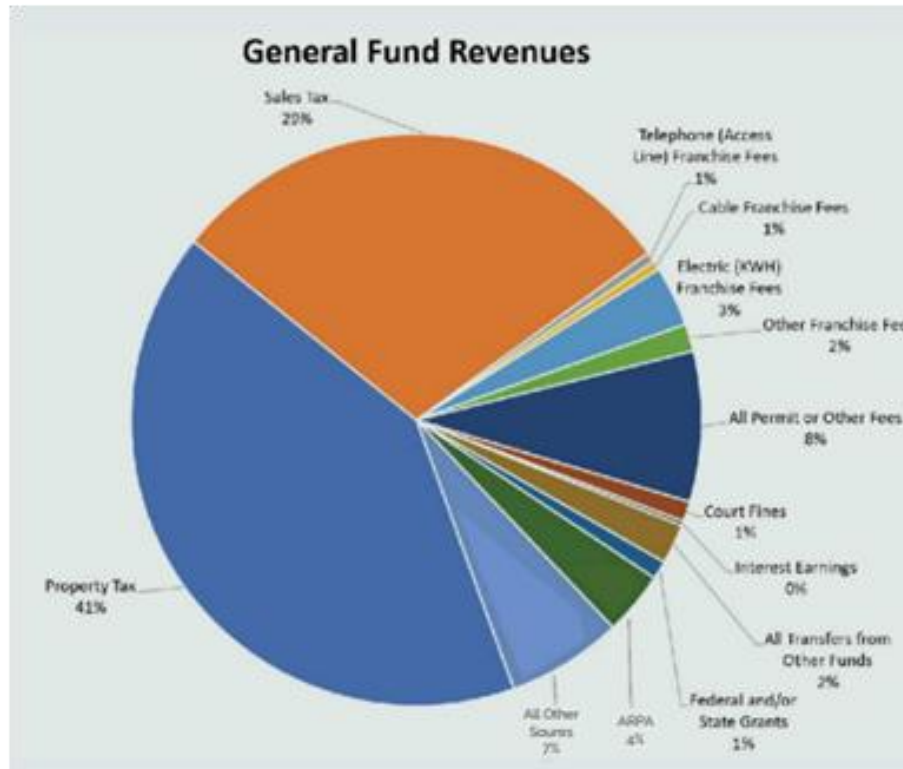
- Local Government Code

- Chapter 102 (Budget)
- Chapter 140 (Truth-in-Taxation Notice)

- Tax Code

- Chapter 26 (Property Tax)

Where do Texas cities get their money?



Source: How Cities Work, Texas Town & City, January 2023, p. 22
<https://www.tml.org/DocumentCenter/View/3452/012023TTC>

Budget and Tax Calendar

- Deadlines When the Tax Rate Does Not Exceed the Voter-Approval Rate

<https://www.tml.org/DocumentCenter/View/3581/2023-Budget-and-Tax-Calendar---Tax-Rate-Does-Not-Exceed-the-Voter-Approval-Rate?bidId=>

- Deadlines When the Adopted Tax Rate Exceeds the Voter-Approval Rate

<https://www.tml.org/DocumentCenter/View/3582/2023-Budget-and-Tax-Calendar---Tax-Rate-Exceeds-the-Voter-Approval-Rate?bidId=>

Texas Comptroller: Truth-in-Taxation

- Index: <https://comptroller.texas.gov/taxes/property-tax/truth-in-taxation/index.php>
- Resources
 - **Truth-in-Taxation Basics Flyer**
 - **Tax Rate Calculations and Worksheets**
 - **Notice Requirements**
 - Hearing Requirements
 - Database/Website Requirements
 - Elections to Approve Tax Rate
 - **Forms for Tax Rate Adoption**
 - **Important Dates**
 - Texas Constitution Provisions
 - **Truth-in-Taxation Videos**

Truth-In-Taxation Basics Flyer

- Key Terms
 - No-New-Revenue Tax Rate (previously, Effective Tax Rate)
 - Voter-Approval Tax Rate (previously, Rollback Rate)
 - No-New-Revenue Maintenance & Operations (M&O) Rate (previously, Maintenance & Operations)
 - De Minimis Rate
 - Unused Increment Rate
- Calculations

Truth-In-Taxation Basics Flyer

- What adopted tax rates trigger an election or petition?

Adopted Tax Rate is:	
BELOW voter-approval tax rate	No election required
ABOVE voter-approval tax rate but BELOW de minimis rate	Voters may petition for an election
ABOVE voter-approval tax rate; Taxing unit does not calculate de minimis rate	Election required
ABOVE voter-approval tax rate and ABOVE the de minimis rate	Election required

Truth-In-Taxation Basics Flyer

- Revenue Threshold in Voter-Approval Tax Rate

Taxing Unit	Voter-Approved Tax Rate
Cities / Counties	3.5%
Special Taxing Units*	8%

*Hospitals, Junior Colleges, and Special Districts with M&O tax rate of 2.5 cents or less.

Unused Increment Rate

- Overview

- The unused increment rate is the three-year rolling sum of the difference between the actual tax rate and the voter-approval tax rate.
- A city may bank any unused amounts below the voter-approval tax rate to use up to three years.

- Calculation

- **Voter-Approval Tax Rate – Actual Tax Rate = Unused Increment Rate**

- Maximum Unused Increment Rate (Three Year Look Back Calculation)

Look back three years

2021 (Year 1)	2022 (Year 2)	2023 (Year 3)	2024
			
1¢	+	2¢	+
		2¢	=
			5¢ (Max)
<p>Taxing unit adopts a tax rate \$0.01 less than the voter-approval tax rate.</p>	<p>Taxing unit adopts a tax rate \$0.02 less than the voter-approval tax rate.</p>	<p>Taxing unit adopts a tax rate \$0.02 less than the voter-approval tax rate.</p>	<p>Taxing unit may adjust the voter-approval tax rate higher by up to \$0.05 without triggering an election.</p>

De Minimis Rate

- Definition: The rate is equal to the sum of:
 - (A) A taxing unit's no-new-revenue maintenance and operations rate;
 - (B) The rate that when applied to a taxing unity's current total value will impose an amount of taxes equal to \$500,000; and
 - (C) A taxing unity's current debt rate.
- Which taxing units calculate a de minimis rate?

Taxing Unit	Yes	No
Small City (population of 30,000 or less)	X	
City (population of 30,000 or more)		X

Flexibility After Disaster

- If a City is affected by a disaster, its governing body may calculate the voter-approval tax rate in the manner provided for a special taxing unit (8%) for up to three years after the tax year in which the disaster occurred.
- Physical damage is required.
- Post-Disaster voter-approval tax rate
 - City has to back out the compounding 8% revenue increases from prior disaster years.
 - Emergency revenue rate is essentially the difference between the previous year's adopted rate and the voter-approval rate calculated as if the taxing unit adopted the 3.5% voter-approval rate at each opportunity during disaster.

Budget & Tax Rate: 2023 Legislation

- **Voter-Approval Tax Rate Calculation – S.B. 2350 (effective June 9, 2023)**
 - Revises the definition of “voter-approval tax rate,” for purposes of the unused increment rate calculation, as a taxing unit’s voter-approval tax rate in the applicable preceding tax year, as adopted by the taxing unit during the applicable preceding tax year, less the unused increment rate for that preceding tax year.
 - According to the bill analysis, this legislation will codify that once the voter-approval tax rate is adopted by the taxing entity, that worksheet may not be changed or adjusted.

Public Purpose Doctrine: Applicable Law

- Texas Constitution Art. 3, § 52
 - “[T]he legislature shall have no power to authorize any county, city, town or other political subdivision of the state to lend its credit or to grant public money or thing of value in aid of, or to any individual, association, or corporation whatsoever. . . .”
- Texas Constitution Art. 11, § 3
 - “No county, city, or other municipal corporation shall hereafter become a subscriber to the capital of any private corporation or association, or make any appropriation or donation to the same, or in anywise loan its credit;”

Public Purpose Doctrine: Overview

- Purpose of Constitutional Restrictions
- Incidental Benefit of a Private Interest
- Three-Part Public Purpose Test
 1. Predominate purpose
 2. Public control over funds
 3. Political subdivision receives a return benefit
- Legislative (City Council) Determination

Public Purpose Doctrine: Examples

Permissible	Impermissible
Payment of benefits to an employee pursuant to an employment contract.	Payment of claim where there is no governmental liability.
Travel expenses for a job applicant.	Reimbursing a private party for their costs incurred in a successful appeal to a zoning board of adjustment.
Chamber of Commerce's use of city resources.	Building a seawall on private property.

Public Purpose Doctrine: Economic Development

- Texas Constitution Art. 3, § 52-a
 - Economic development is a public purpose
 - Local Government Code, Chapter 380
- Three-Part Public Purpose Test
 1. Outline steps business will take to justify public funding
 2. Claw back provision if obligations not met
 3. Tangible means of measuring whether business has met obligations

Municipal Borrowing: Authority

- Texas Constitution Art. 11, §§ 5 and 7
 - Generally, levy and collect tax to pay interest and create a sinking fund of at least two per cent to repay principal
 - A “**sinking fund**” is a fund into which moneys are placed to be used to redeem securities in accordance with a redemption schedule in a bond contract.
 - Remember, constitutional and statutory limits on a city’s power to tax; additional taxes for bonds plus other taxes may not exceed these restrictions
 - Since 2011, cities and counties may enter into multi-year interlocal agreements

Municipal Borrowing: Authority

- Texas Constitution Art. 3, § 52
 - **City must have specific authority to issue bonds for a specific purpose**
 - Legislature has authority to allow cities to issue bonds
- Texas Supreme Court: *McNeill v. City of Waco*
 - Defines “debt”
 - Exceptions:
 1. **Current revenue**
 2. **Special funds**

Municipal Borrowing: Authority

- Authority derived from:
 - **Constitution**
 - **Statutes**
 - Texas Government Code § 1331.052
 - General authority for home rule cities
 - Permanent public improvements
 - Other public purposes authorized by charter and consistent with constitution
 - Additional Statutory Authority
 - **Home Rule Charter**

Municipal Borrowing: Bonds

- **Definition:** A promise by a local government (issuer) to lenders of money (investors) to repay that money (principal) along with interest, by a certain date (maturity)

Types of Debt: General Obligation Debt

- **General Obligation (G.O.) Bonds**
 - Statute: Texas Government Code, § 1331.052
 - Backed by ad valorem taxes
 - Authorized by municipal bond election
 - Used for permanent public improvements and other public purposes as provided by statute and city charter
- **Certificates of Obligation (C.O.)**
 - Statute: Texas Local Government Code, Ch. 271
 - Supported by ad valorem taxes, revenues or both
 - Election is *not* required (unless a petition is received)
 - May be used to pay for: public improvements, professional services, demolition of substandard structure, restoration of historic structures
- **Time Warrants**

Types of Debt: Revenue Bonds

- Authority from various statutes according to the type of project
- Not secured by a pledge of property taxes
- No bond election required (unless city charter requires)
- Revenue stream is pledged to finance a revenue-producing asset, often a utility

Other Types of Debt

■ Refunding Bonds

- Statute: Texas Government Code, Ch. 1207
- A pledge of ad valorem taxes, revenue or both unless limited by applicable statute
- Bond election is *not* required
- May be used to refinance short-term or long-term debt, or other obligation

■ Judgment Bonds

- Statute: Texas Government Code, § 1507.001
- Bond election is required
 - Pursuant to Texas Government Code, Ch. 1207, can refund an obligation to pay pursuant to a court judgment without an election.
- Issued to pay final judgments against a city if money is not available to pay the judgment

Other Types of Debt

- **Lease-Purchase Agreements**
 - Statute: Texas Local Government Code, § 271.005
 - Used to finance the purchase of personal property
- **Anticipation Notes**
 - Statute: Texas Government Code, Ch. 1431
 - Issued to borrow against anticipated revenue, typically federal grant money
- **Tax Note**
 - Statute: Texas Government Code, § 1202.003
 - Tool for alleviating short-term cash flow needs

Municipal Borrowing: Role of Attorney General

- **Statute:** Texas Government Code, Chapter 1202
- **Generally**
 - Submission of the public security and the record of authorization proceedings to the Attorney General for review and approval
 - A public security cannot be issued if it is not approved by the Attorney General
 - After approval, registration by the comptroller, and issuance, public security is incontestable, except for claim of unconstitutionality
- ***Noteware v. Turner (2019)***

Municipal Borrowing: Other Roles

- **Bond Counsel** – prepares documents, submits the bonds to the Attorney General for approval, ensures compliance with state and federal law; provides a bond opinion regarding validity and tax-exemption
- **Financial Advisor** – works with the issuer to structure bond financing; works with the Underwriters to price and sell the bonds; assists issuer in preparation of Official Statement; fiduciary obligation to the city
- **Underwriters** – purchase all of an issuer's bonds and resells the bonds in the market to investors
- **Finance Director** – understands financial restraints of city and debt capacity (ability to sell debt and cover debt service within tax or revenue constraints); tracks bond election authority and bond proceeds expenditures; budgets adequate interest and sinking fund to pay debt service
- **City Attorney** – addresses traditional municipal legal issues at outset (charter provisions, competitive bidding, contracts); identifies legal issues during the life of bonds (use of proceeds, use of facilities)

(Source: <https://www.msrb.org/sites/default/files/Financing-Team.pdf>)

Legal Framework: Calling a Bond Election

- **Election Date:** Bond election may be held on any uniform election date (May or November).
- **Facilities Plan:** A Facilities Plan along with the estimated cost should be prepared and presented to the City Council, typically four to five months prior to calling the election.
- **Citizen Committee:** A Citizen Committee may be formed to make recommendations to the governing body on the Facilities Plan and/or be involved after the election is called to advocate for/against the bond election. The Citizen Committee should be made up of citizen volunteers. No public funding should be provided to the Committee. City resources cannot be used to campaign for or against the bond proposition. The City can only give factual information regarding the bond election without promoting a “Yes” or “No” vote.
- **Ballot Language:** Engage bond counsel to draft language for staff and city council review. Seek Attorney General’s preapproval of the proposition language to ensure the eventual approval of the bonds’ issuance by the Attorney General.
- **Election Ordinance (Order):** A bond election may not be ordered earlier than the 90th day before the election day and not later than the 78th day before the election day.

Municipal Borrowing: Bond Proceeds

- Bond proceeds can only be spent for the purposes for which they were issued:
 - Capital expenditures
 - Election proposition restrictions
 - Purpose clauses
- Expenditures must be tracked for continuing compliance with federal tax law

Municipal Borrowing: 2013 Legislation

- **Bond Election Orders**
 - **Legislation: S.B. 637 (effective September 1, 2013)**
 - **New requirements**
 - Additional information in debt obligation election order
 - Posting of debt obligation election order:
 - At each polling location
 - In three public places in the municipality
 - On municipality's Internet website, if municipality maintains a website
 - **Amended by H.B. 477 (effective September 1, 2019)**

Municipal Borrowing: 2015 Legislation

- **Local Debt Reporting**
 - **Legislation: H.B. 1378 (effective January 1, 2016)**
 - **New requirements**
 - Annually compile and report certain financial information
 - May provide a link to separately posted information
 - Alternates to preparing a report
 - Annual report be available for inspection and posted on website

Municipal Borrowing: 2015 Legislation

- **C.O.'s**
 - **Legislation: H.B. 1378 (effective January 1, 2016)**
 - City may not issue C.O. if voters voted down bond proposition for the same purpose within the past three years
 - Exceptions: for public calamity, to protect public health, for unforeseen damage to public equipment/property, or to comply with state or federal law

- **Capital Appreciation Bonds**
 - **Legislation: H.B. 114 (effective September 1, 2015)**
 - Establishes new requirements for a city to issue capital appreciation bonds that are secured by property taxes
 - These requirements do not apply to refunding bonds or capital appreciation bonds for transportation projects.
 - **Amended by H.B. 295 (effective September 1, 2017)**

Municipal Borrowing: 2017 Legislation

- **Capital Appreciation Bonds**
 - **Legislation: H.B. 295 (Effective September 1, 2017)**
 - Cleans up a drafting error in H.B. 114 and provides that refunding bonds and capital appreciation bonds issued for transportation projects are exempt from the restrictions in *all* of Section 1201.0245, Texas Government Code.

Municipal Borrowing: 2019 Legislation

- **Local Debt – H.B. 440 (effective September 1, 2019)**
 - If city has a website, prominently post during the 21 days before G.O. bond election day any **sample ballot**, along with **notice of election** and **contents of proposition(s)**.
 - A city may not issue a G.O. bond if weighted average maturity of the issue of bonds exceeds 120% of the reasonably expected weighted average economic life of the improvements or personal property financed.
 - **Unspent proceeds** of issued G.O. bonds only:
 - For specific purpose for which bonds authorized;
 - To retire the bonds; or
 - For another purpose if
 - Specific purpose accomplished or abandoned; and
 - Voters approve the use of proceeds for the proposed purpose.

Municipal Borrowing: 2019 Legislation

- **Local Debt – H.B. 477 (effective September 1, 2019)**
 - **Election Order**
 - **Form of Ballot**
 - **Voter Information Document**
 - On election day and during early voting, in a prominent location at each polling place;
 - No later than the 21st day before the election, in three public places in the city limits; and
 - During the 21 days before the election, on the city's website.
 - **C.O.'s**
 - Timeframe for newspaper notice of intention to issue a C.O. is now 45 days.
 - Post intention to issue a C.O. on city's website at least 45 days before the passage of the C.O. issuance ordinance/order.
 - Elements of notice of intention to issue a C.O.

Municipal Borrowing: 2019 Legislation

- **Bond Propositions – S.B. 30 (effective September 1, 2019)**
 - **Each single specific purpose** for which bonds requiring voter approval are to be issued shall be printed on the ballot as a separate proposition.
 - A proposition may include as a specific purpose one or more structures or improvements serving the substantially same purpose and may include related improvements and equipment necessary to accomplish the specific purpose.
 - A proposition seeking approval of the issuance of bonds shall specifically state:
 - Plain language description of the single specific purpose for which bonds are to be authorized;
 - Total principal amount of the debt obligations to be authorized; and
 - That taxes sufficient to pay the principal and interest on the debt obligations will be imposed.
 - All Bond Counsel letter, dated December 27, 2019, from the Public Finance Division of the Office of the Attorney General of Texas regarding single specific purpose requirement.

Municipal Borrowing: 2021 Legislation

- **Debt Financing – H.B. 1869 (effective September 1, 2021)**
 - Revises the **definition of “debt”** for purposes of the debt service property tax rate calculation to only include debt that meets one of the following requirements:
 - Has been approved at an election;
 - Includes self-supporting debt;
 - Evidences a loan under a state or federal financial assistance program;
 - Is issued for “designated infrastructure”;
 - Is a refunding bond;
 - Is issued in response to an emergency related to a hurricane or tropical storm;
 - Is issued for renovating, improving, or equipping existing buildings or facilities;
 - Is issued for vehicles or equipment; or
 - Is issued for a tax increment reinvestment zone or a transportation reinvestment zone.

Municipal Borrowing: 2023 Legislation

- **Local Debt – H.B. 4082 (effective September 1, 2023)**
 - Defines “public work” for purposes of a certificate of obligation by a city or county
 - This term was previously undefined in the statute
 - See All Bond Counsel Letter, dated November 1, 2023 for guidance from Attorney General’s Office
(<https://www.texasattorneygeneral.gov/sites/default/files/files/divisions/public-finance/ABCLetter-11-01-2023.pdf>)
- **Bond Review Board Assistance – H.B. 1038 (effective September 1, 2023)**
 - Requires cities to submit any information to the Bond Review Board (<https://www.brb.texas.gov/>) necessary for the Board’s preparation of the Biennial Report on State Lending and Credit Support Programs to the legislature.

Municipal Depositories

- **Statutes**
 - Local Gov't Code, Chapters 105 and 131
 - Gov't Code, Chapter 2257

Municipal Depositories: Requirements

- City Council must designate bank, credit union, or savings association that will serve as the depository for municipal funds
- Designated officer
- Institutions not located in city
- Depository services agreement requirements
- Special depository

Municipal Depositories: Conflicts of Interest

- **Statute:** Texas Local Government Code § 131.903
- **10% Rule:** A city may *not* select a depository if:
 - one or more municipal officers or employees, who have a duty to select the depository, own or have a beneficial interest, individually or collectively, in more than 10% of the outstanding capital stock of the bank
- Home-rule charter provision may supersede
- Contrast with Local Gov't Code, Chapter 171

Municipal Investments

- **Statute:** Public Funds Investment Act (“PFIA”) (Gov’t Code, Chapter 2256)

Municipal Investments: Requirements

- City must comply with Public Funds Investment Act (PFIA) to invest public funds
- PFIA:
 - Written investment policy
 - Include list of authorized investments
 - Only invest in authorized list
 - City official must complete training regarding PFIA
- No penalty provision, but may impact credit ratings or result in negative comments in an audit

Municipal Investments: 2023 Legislation

- **Repurchase Agreements – S.B. 1246 (effective June 18, 2023)**
 - Allows for repurchase agreements using a joint account

Questions?