Current Municipal Bond Procedures in Minnesota

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In an article published in the Minnesota Law Review in May, 1936,1 the writer pointed out that Minnesota then had the foundation of a workable code of procedure governing the issuance of municipal bonds but that the law needed considerable revision. Since that time, due largely to the work of Mr. William B. Henderson, Code Revisor, the necessary changes have been made in the code so that now Minnesota has one of the best municipal bond codes which can be found in the laws of any state.2 Except for certain "special" amendments relating to schools, discussed hereafter, this statute has been kept relatively free from the kind of crippling amendments which tend to obscure the simple procedure. The procedure required to comply with the Minnesota bond code for general obligation bonds may be summarized as follows:

1. A resolution by the governing body determining to issue bonds and calling an election.
2. Notice of election by posting and publication.
3. Holding and canvassing the election.
4. Resolution of the governing body determining to sell bonds, fixing the amount, maturities and other details.
5. Notice of sale of bonds published ten days in advance in the official newspaper and in a financial paper.
6. Meeting of the governing body to consider bids, award the bonds, fix the bond form and levy taxes.
7. Filing of the tax levy resolution with the county auditor and obtaining the certificate.
8. Printing, execution and delivery of the bonds.

A first problem is the determination of the debt limit. The Minnesota Constitution does not contain any debt limitation relating to municipal corporations—the only limit on municipal borrowing is that fixed by statute.3 This contains two basic debt limits; the 50% limit relating to school districts and the 20% limit relating to all other types of municipalities. The remaining portions of Section 475.53 are actually special laws which relate only to one or at most a few situations.4 The 20% debt limit applying to municipalities generally is computed by considering the various

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4. Subd. 3 is a special limit applying to Minneapolis. Subd. 5 applies only to Duluth school district. Subd. 2 and Section 475.533 applies to certain villages and school districts receiving apportionment of gross earnings taxes.
deductions provided in Section 475.51, subd. 4. The resultant "net
debt" may not exceed 20% of the assessed value.

Assessed value for purposes of the debt statute is defined in
Section 475.51, subd. 5, as the value upon which taxes are levied.
The fair market value of property is computed by the local assessor
as the "full and true value." In actual practice this "full and true
value" has been 30% or less of the market value due to the un-
willingness of local assessors to value property at its fair value.
These values are then equalized by the local board of review, by
a county board of review and finally by the State Tax Commission.
After the State Tax Commission has passed upon this value it is
then subjected to certain percentages. Under Section 273.13 differ-
et kinds of property are valued for taxation at different per-
centages of the full and true value. This value upon which taxes
are then levied is not defined in the taxing statute, but in the bond
code it is referred to as "assessed value." The 1955 legislature
adopted two amendments to Section 475.53, subd. 4, which changed
the meaning of "assessed value" for computing the debt limit of
school districts. The Attorney General ruled that under Chapter
656 the "assessed value" for computing bonded debt of school dis-
tricts was to be determined by including the full and true value of
homestead properties, but in a test suit the Supreme Court
held that this assessed value was to be determined by valuing homestead
properties as though they were non-homestead properties. The
result was to give a much smaller increase in the borrowing powers
of school districts than would have been possible under the inter-
pretation of the Attorney General. The other amendment to Sec-
tion 475.53, subd. 4 (Chapter 304) sought to enlarge the debt limit
by permitting certain districts to add the value of buildings under
construction during the current year.

Both amendments were adopted for the obvious purpose of per-
mitting school districts to incur debt in an amount in excess of 50%
of the "assessed value" as defined in Section 475.51, subd. 5, and illustrates the difficulty in setting fixed debt limits. Many other

5. Minn. Stat. §§ 272.03(8), 273.11-273.12 (1953)
7. This classification statute has been considered by the Minnesota Supreme Court in Phelps v. Minneapolis, 174 Minn. 509, 219 N. W. 872 (1928), Apartment Operators Ass'n v. Minneapolis, 191 Minn. 365, 254 N. W. 443 (1934).
laws of special application have been passed by the legislature for
the same purpose. In view of this practice it is doubtful whether
there is any value in a statutory debt limit which can be so easily
changed whenever it actually restricts borrowing by a municipality.

In order to determine whether the debt limit will be exceeded,
the principal amount of all bonds must be included and all sinking
funds must be deducted.12 The debt of other municipalities which
occupy part or all of the same territory is not included. Our Supreme
Court has held that the debt of a previously existing school district
which became part of a reorganized or consolidated district may be
excluded.13 Since the value of taxable property during the current
year is ordinarily not determinable until December or later, it is
necessary to rely upon the assessed value for the previous year.
During a period when assessed values were dropping this may
present a serious problem. However, in recent years it is ordinarily
assumed that the assessed value for the current year will be at least
as high as the value for the previous year.

A connected question involves the amount which should be
stated in the proposal submitted to the voters. Since no debt limit
is created by the vote, the debt limit becomes important only at the
time the bonds are delivered. At that time bonds may be issued
up to the full amount permitted by law even though the voters have
authorized a debt which would exceed the debt limit.14 The Attor-
ney General has suggested a possible limitation to this rule, pointing
out that the governing body must carry out substantially the pro-
posal which the voters approved.15 If the amount of bonds which
can be issued would not accomplish the purpose which the voters
approved, the use of the funds for a different purpose would be
open to question.16

Bond proceedings are initiated by a resolution of the governing
body stating the amount proposed to be borrowed and the purpose
for which the debt is to be incurred.17 The term "purpose" is ex-
pressed in the singular. The statute requires that each purpose shall
be submitted so that the voters can express their wish for or against
incurring debt for the single purpose only. If the proposal combines
more than one purpose it would be invalid. Sometimes this presents

13. Huffman v. Ind. Con. School Dist. 11, 230 Minn. 289, 41 N. W 2d
455 (1950).
14. State v. Trask, 155 Minn. 213, 193 N. W 121 (1923), Annot. 175
A. L. R. 823 (1948).
15. Att'y Gen Opinion to Dean M. Schweickhard of July 1, 1955.
a troublesome question and there are many cases in which the court has had to determine whether the particular purpose was singular or multiple. So far as school districts are concerned, this problem will not ordinarily arise since every court which has passed upon the question has held that various improvements to a school system present but a single question. The question often arises whether the proposal submitted to the voters should include the statement of such details as bond maturities, maximum interest rate, call provisions and place of payment. The statute does not require that these details be stated and therefore it is unwise to include them. Even where not required the governing body may be bound by details which were presented to the voters in the election proceedings.

Bond elections must be held in accordance with statutes relating to municipal elections. School meetings and elections are governed by Sections 124.01 to 124.09. These sections preserve the distinction between informal school meetings in common districts and the more formal elections in independent districts. In independent districts the polls must be open at least one hour and may not remain open more than twelve hours. In most school elections it is the practice to have the polls open in the evening hours. For special school meetings or elections the statute requires one week's published notice if there is a newspaper published in the district. Ten days posted notice is also required for all school elections.

The governing body should meet after the closing of the polls to canvass the results. Section 208.07 provides for a contest of an election by proceedings commenced within ten days after the canvass is completed. This is the exclusive remedy for contesting the validity of those elections which have been called or conducted in a legal manner. Prior to 1955 there was no appeal from school district elections, but the 1955 legislature provided that such elections may be appealed in the same manner as other municipal elections.

Note that this case was decided on the peculiar form of submission and is not opposed to the general rule.
24. Minn. Stat. § 124.06 (1953) (Schools), § 212.69 (Cities), § 212.36 (Villages), § 205.16 (Counties).
Therefore, in school as in other elections the canvass should be promptly made so that the ten day appeal period will expire prior to the time bonds are offered for sale.

After an election has been held and the municipality has the authority to issue bonds, the question arises as to how soon the bonds should be sold. The governing body is not required to issue bonds immediately. A delay of four years will not invalidate the issue. On the other hand, at least six weeks will be required in order to get the bonds sold and delivered, and this time should be taken into consideration in considering when the proceeds will be needed. Since the municipality cannot take bids on the work until the voters have given the necessary authority, it usually happens that several months will elapse before the bond proceeds are needed; and it is advisable to wait until this time before the bonds are offered for sale. The interest rate may change in the meantime, but at the very least the municipality will have saved the interest on the bonds during the period before the bonds are delivered and this is likely to offset any unfavorable change.

Should the municipality sell the entire authorized amount of bonds at one time? The answer to this question will depend upon the size of the issue and the time when the balance of the funds will be needed. If the issue is less than $200,000, the entire amount should probably be sold at one time. In the case of larger issues it may be advisable to sell the bonds in two installments. This will have the double advantage of keeping the supply of bonds low and thus improving the market, and it will also save interest on the remainder of the bonds upon which the sale is delayed. Bonds should not be offered for sale more often than at six month intervals and this should also be taken into consideration.

The bonds must be advertised for sale ten days in advance of the date of sale in the official newspaper and in a financial paper published in a city of the first class. It is the common practice in Minnesota to use Commercial West (published in Minneapolis) as the financial paper. The Bond Buyer published in New York City is of the same general character; but since Minnesota bonds are not very frequently sold in the New York market, comparatively few sales in this state are advertised in that paper. In any case it gives news of all sales even though they are not specifically advertised.

In order to sell municipal bonds to investors generally it is,

necessary to obtain the opinion of certain firms of attorneys who are recognized by dealers as "municipal bond attorneys." Certain opinions are accepted nationally and others are accepted for bonds of a certain area. Here it is necessary to obtain the advice of investment dealers. It is seldom wise to attempt to sell bonds on the opinion of the municipal attorney alone even if he is thoroughly experienced in such matters. Usually it is best to have the proceedings prepared by the local attorney after conference with the attorney whose opinion is to be furnished when the bonds are sold.

The formal advertisement does not take the place of the financial information which must be supplied to interested parties. This should include not only a description of the bonds and the source for their payment and the assessed value of taxable property but it should also include complete financial information so far as it is available. The prospective purchasers will want to know the amount of outstanding bonds of the municipality, the amount of all funds on hand, the income of the municipality from taxes and other sources and the amount of any debt of municipalities with overlapping boundaries.

The bonds must have serial maturities with part falling due annually or semiannually, and the largest amount maturing in any year after the third year may not be more than five times the smallest amount maturing in any preceding year excepting the first two years. Within these restrictions the maturities may be fixed by the governing body but should be made as short as possible, taking into consideration the required tax levies. If other things are equal the lower the average maturity the lower the interest rate. If the bonds mature in ten years they can be sold at a better rate than fifteen or twenty year bonds. If it is necessary to extend the maturities for thirty years, this is sure to be reflected in the rate received. The bonds should mature in approximately equal amounts each year although it is a common practice to increase the installments in later years so that the tax levies will be approximately equal. If it is possible the annual installments should be in amounts of five thousand dollars or some multiple thereof since banks and other financial institutions like to get blocks of bonds. In fixing the earliest maturities the time when taxes are collected must be taken into consideration. Taxes are levied in the fall and collected during the following year. A very small amount is available prior to the middle of the following year and the second half is not available.

until the end of the following year. For this reason it is unwise to have bonds mature earlier than the end of the calendar year following their issuance, and it is usually advisable to take advantage of the statutory provisions which permit the postponing of the first maturity for three years in order that the first levies can be kept at a minimum in spite of the necessity for covering two years interest.

All bonds should be in one thousand dollar denominations if that is possible. Bond purchasers do not readily accept bonds with other denominations. Even if the total amount does not evenly divide into one thousand dollars, it is better to have a higher amount mature in some years than in other years in order to keep the bonds in one thousand dollar denominations. The bonds should be dated on the first day of some month which need not necessarily be the month in which the bonds are sold. Since the bonds cannot be delivered before their formal date this date should not be too long after the date of the sale. Usually the bonds mature on the anniversary date of the date of issue although this is not required; also the maturity date should be fixed with some reference to the time that taxes are collected. If the maturity date is other than the anniversary date it should be nine months, six months or three months later in order to simplify the problem of the bidder in computing the interest cost. The interest should be made payable semiannually on the maturity date and at the six months interval and should be represented by separate detachable coupons.

A practice has developed in recent years for bids to provide that the bonds will bear a higher interest rate during the first year or two, the additional interest being represented by separate coupons. This practice is not specifically authorized by statute but is believed to be lawful, provided that it is properly expressed as a division of the interest payments, and not as the payment of additional or supplemental interest. The effect of such a bid is to require the municipality to pay an extra amount of interest during the first year, and a question may arise whether such a bid is more favorable than a bid which would require somewhat higher total interest but spread over the life of the bonds.

Unless the municipality reserves the right to redeem its bonds it has no right to pay them until the stated maturity date. Redeemable bonds are not desirable from an investor's standpoint, and

30. Minn. Stat. § 276.11 (1953). The county treasurer is required to make settlement on the last day of February, May and October. However, the settlement day is usually delayed by six weeks or more.

serious consideration should be given to the question whether there is sufficient value in reserving the right to call bonds before their maturity date. It is rarely desirable to make the bonds subject to redemption earlier than five years except at a premium since such bonds would have little interest to investment dealers who furnish the big market for municipal bonds.

The purchaser should be permitted to designate the bank where the bonds will be made payable. Unless the bonds are payable at a central bank which maintains a department for this purpose, they are not desired by many investors, and the municipality will have to pay a higher rate for the privilege of paying the bonds at the office of its treasurer or at a local bank.

At the meeting at which the bonds are sold the form of bonds should be fixed by resolution of the governing body. It is important to fix the form for purposes of identification and also to provide the recitals which make the bonds easily negotiable. The officers should also be authorized to prepare and sign the bonds. The bonds may be signed manually by one officer and by the facsimile signature of another officer. It has become increasingly common to have the bonds signed manually by the clerk with the facsimile signature of the mayor or chairman. In every case the facsimile signatures are printed on the coupons.

The statute provides for registered bonds but they are seldom used in Minnesota. Most bonds are held as bearer bonds. This registration is not to be confused with the registration required to be made by the county auditor. That registration is for the purpose of identifying the bonds and establishing the fact that a tax levy has been made as required by law. A certified copy of the resolution levying taxes must be delivered to the county auditor. He then makes a notation showing the amount of the issue, the interest rate and maturities and delivers a certificate that the bonds have been entered on his bond register.

Where bonds are subject to redemption it is customary to provide for an additional registration of the names of holders of redeemable bonds for the purpose of mailing notice of redemption. The statute provides that bonds may be made redeemable upon such notice and at such time and at such price as determined by the governing body. The usual practice is to provide for thirty

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days mailed notice to the bank where the bonds are payable and to all bondholders whose names, addresses and bond numbers have been registered with the clerk.

After the bonds have been sold the municipality must arrange to have the bonds printed. This is best done by printing houses which specialize in this kind of work. Most investors are acquainted with certain instruments which they identify as municipal bonds. Instruments which are printed in any other form are not readily acceptable. Furthermore, there is great danger of an error in the bond form or coupons if the printing is handled by printers who are not skilled in this type of work.

A question which is often asked is what interest rate may be expected when the bonds are sold. The interest rate changes from time to time, depending on the action of the federal government through the federal reserve banks and other agencies. It also depends upon the supply of bonds of the particular kind. Therefore, it is impossible to predict exactly what interest rate will be received. However, if the municipality offers bonds of the kind which the investors are seeking and furnishes full information it can be assured of a low interest rate as compared to borrowing by any other type of borrower. This low rate arises from the fact that municipal bonds are exempt from present federal income tax.

This article has been somewhat simplified by limiting the discussion to fully tax supported general obligation bonds. The more complicated procedure required for the issuance of special assessment bonds under Minn. Stat. Chap. 429 (1953) has been adequately discussed in the article by DeForest Spencer, Jr. in 38 Minn. Law Review 582. Another type of obligation has come into increasing use during the past few years. This is the bond payable solely from revenues of a municipal enterprise. Our Minnesota statutes do not adequately set forth the requirements for this type of obligation and the local attorney should not attempt to prepare proceedings for a revenue issue without the help of an experienced expert.

In the writer’s opinion, satisfactory proceedings for municipal bonds of the type discussed in this article can be prepared by any competent attorney. However, it is essential that care be exercised in the adoption of all the procedural steps and these should only be done under the supervision of the municipal attorney. No “expert” should be permitted to come between the municipality and its legal advisor. On the other hand, with reasonable care in checking the applicable statutes before drafting papers, the attorney should have
no difficulty in preparing satisfactory proceedings. About all an expert can do is to help the attorney to find all of the applicable statutory provisions which have to be followed.

In drafting proceedings it is necessary to bear in mind the fact that municipal corporations have only limited powers. Express statutory authority is ordinarily necessary before the action can be taken. While there has been a considerable improvement in the Minnesota Statutes since the adoption of a system of a permanent code revisor, there is still need for considerable improvement in the chapters relating to municipal corporations. It is still necessary to check all of the chapters between 410 and 475 to be sure that no applicable statute has been overlooked. In addition, the attorney should check the election statutes from Chapters 200 to 212 and if the proceedings involve a school, it is necessary to examine Chapters 120 to 128.

The requirements of the statute should be rather strictly followed. On the contrary, anything not required by statute should ordinarily be no part of the official proceedings. In the opinion of the writer it is unwise to encumber the proceedings with extraneous matter or excessive details covering the plan for the municipal building or improvement.