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TO: COUNCIL MEMBERS

FROM: David Whitaker, Director
Legislative Policy Division 

DATE: October 30, 2018

RE: Report on LPD Response to Council Member Raquel Castaneda-Lopez Questions Regarding Bond Issuance and Refinancing

On October 22, 2018 Council Member Raquel Castaneda-Lopez through Council President Brenda Jones, requested that the Legislative Policy Division (LPD) respond to the following questions regarding the Bond Authorizing Resolution¹:

1. Historically, how has the issuance and refinancing of bonds been handled? Have specific capital projects been included within the Resolution beyond the voter-authorized categories?
2. What level of specificity is needed to put bonds out to market and refinance?
3. If specific capital projects are included in a bond authorizing resolution, is the administration still required to come before Council and request a budget amendment before moving forward with a project?

Detailed below are LPD's responses to Council Member Castaneda-Lopez's questions.

- 1. Historically, how has the issuance and refinancing of bonds been handled? Have specific capital projects been included within the Resolution beyond the voter-authorized categories?**

¹ Bond Authorizing Resolution – UTGO bonds, Series 2018 and Refunding Bonds, dated October 12, 2018

The Administration through the OCFO and Bond Counsel prepares a Bond Resolution when the City wants to issue bonds that were authorized by the voters or refinance current debt obligations. The Bond Resolution is submitted to City Council for review and approval. After City Council approval is received the City sells the bonds to underwriters who market the bonds to investors.

In the past the City used the general categories of the voter approved bond authorizations to describe the capital projects to be funded². Historically, in most cases that we reviewed, the issuance of UTGO bonds has occurred without designating specific projects beyond the broad categories authorized by voters through ballot proposals. Using general descriptions provides the City with more flexibility on what projects can be funded by the bond proceeds.

The OCFO representatives told us that the projects were detailed in Exhibit A of the Bond Resolution for transparency and to encourage more demand for the purchase of the bonds, especially with the City re-entering the market after bankruptcy.³

2. What level of specificity is needed to put bonds out to market and refinance?

Specificity of the purpose for what the bond proceeds will be used for can be general or detailed depending on what the bond investors will demand. The City's Bond Counsel and Financial Advisors would recommend the specificity needed. It is our opinion that municipalities with lower credit ratings such as Detroit would need to provide more detail to investors to create sufficient demand and favorable interest rates for the bonds. The City's Bond Counsel and Financial Advisors would be able to provide a more informed response to this question.

In Exhibit A to the new 2018 UTGO bond resolution some of the projects were detailed and some were not. For example, a more specific project is the Charles H. Wright Museum roof replacement projected to cost \$1.0 million and a less specific project is the land acquisition and preparation for future industrial development projects projected to cost \$26.1 million.

From LPD's report⁴: "Some Councilmembers have expressed their desire to have the opportunity to modify the list of recommended projects that is a part of the bond resolution so that the list of

² The following is an example of general categories to describe bond proceeds. Bond Resolution for 1997 A&B UTGO Bonds dated October 28, 1997, Article III Section 301 (b) "Bonds of the City aggregating the principal amount of not to exceed Thirty Four million Two Hundred Fifty Thousand Dollars (\$34,250,000), shall be issued for the purpose of financing certain portions of the costs of the City relating to the following Prior Voter Authorized Projects in the following not to exceed amounts as previously appropriated by the Council: (i) \$12,000,000 for Neighborhood/Economic Development; (ii) \$7,000,000 for Recreation-Park Development; (iii) \$1,000,000 for Fire-Buildings and Sites; (iv) \$10,000,000 for Public Lighting System Betterments, Improvements and Extensions; (v) \$2,000,000 for Zoo Improvements; and (vi) \$2,250,000 for the Detroit Institute of Arts improvements, and paying all of a portion of the costs of issuance of such bonds."

³ Bonds can contain covenants such as requirements that the proceeds be used for a specific purpose. If such covenant was included in a bond document the City Council would be unable to approve any contract or budget amendment not in accordance with the covenant without risking adverse legal action.

⁴ Resolution (1) Authorizing the Issuance of Not to Exceed \$255,000,000 in Unlimited Tax General Obligation Bonds, Series 2018 for the Purpose of Paying the Costs of Certain Public Improvements; and (2) Authorizing the Issuance of Not to Exceed \$500,000,000 in Limited Tax General Obligation Refunding Bonds for the Purpose of Refunding All or a Portion of the City of Detroit's Outstanding Financial Recovery Bonds, Series 2014B, Financial Recovery Income

capital projects would be more reflective of Council's priorities before Council's vote on the bond resolution. John Hill, CFO, provided LPD the following regarding this issue:

There are two tests to make sure that projects are in accord with borrowing. They have to fit both the purposes of the voter authorization and the requirements of capital in the IRS regulations. To price the bonds we have to match the length of bonds to the useful life of the projects and this is a real balancing act that has already been done for these projects. If we issue bonds under this authority and then change out projects it can be done but a lot of work will have to go into making sure the new or substitute projects meet the three requirements. We simply do not have the time to do that and make a Dec 31 date which is important for all the reasons we provided earlier.

The approval of the resolution would not lock in projects for the next 2 years. However some of these projects are multi year and we would not want to start them if we did not know we had the authority to finish them. The rating agencies and investors will be looking for those assurances as well.

The council has a couple of opportunities to affect the projects that are worked on. Clearly they will have the Capital Agenda in front of them on Nov 1 and are able to express their support or priority for various projects during that process⁵. They also have control over all the Contracts that come out of the bond sale as they will have to be approved by the body. We heard the Council prior to this process and accordingly included a number of projects the Council expressed concern with our finding funding to support. We did that because of the lead time necessary to validate the projects as I have explained above. I believe the process that was used incorporated a number of different priorities and was respectful to concerns of the Council.

There is money left over in bond authorization⁶ for Council priorities.”

3. If specific capital projects are included in a bond authorizing resolution, is the administration still required to come before Council and request a budget amendment before moving forward with a project?

LPD asked the OCFO: “If Council approves the new money UTGO bond sale, will the OCFO present to Council a budget amendment to appropriate the bonds in the City’s FY 2019 budget and show the impact on the four-year financial plan?” The OCFO’s response to this question was: “The Resolution itself serves this purpose.”⁷ As a result, the OCFO will not submit a budget amendment in FY 2019 for City Council to approve the appropriation of the estimated \$48.2

Tax Revenue and Refunding Bonds, Series 2014A, and Financial Recovery Income Tax Revenue and Refunding Bonds, Series 2014B, dated October 22, 2018.

⁵ It is important to remind the Council that the Capital Agenda is a planning document and not a capital budget.

⁶ Attachment III in LPD’s report dated October 22, 2018 indicates there would be approximately \$28.9 million remaining in bond authorization for public safety and recreation/libraries/museums/zoo type capital projects, if Council approves the proposed bond resolution currently before you.

⁷ LPD report dated October 22, 2018 on the bond resolution, Attachment IV “LPD’s Questions Regarding the Proposed UTGO Bond Sale and LTGO Refunding Bond Sale, Question 12 on page 7.

million for the recommended capital projects for FY 2019 to be funded by the 2018 UTGO bond proceeds.

We asked the City's Budget Director on October 25, 2018: "Can you provide me with the Charter reference or legal reference that gives the Bond Resolution the authority to appropriate funds for capital projects and not have to submit a budget amendment for the appropriation? Essentially can you provide justification for your stance at the City Council hearing on Tuesday that a Budget Amendment is not required to appropriate the capital project funds for FY 2019 that will be financed by the new UTGO bonds?"

The Budget Director responded as follows: "Section 1002. Approval of Other Documents and Actions; Treasury Approval. The Authorized Officers, the City Clerk and any other officers or employees of the City are hereby authorized and directed on behalf of the City to take any and all other actions, perform any and all acts and execute any and all documents that shall be required, necessary or desirable to implement this Resolution."⁸

The Administration in the past sold general obligation bonds on a regular basis. After the bonds were sold, the capital projects for a given fiscal year were either already a part of the budget for that given fiscal year, or the Administration had to present a budget amendment to Council to budget the capital projects and the proceeds of the bond sale as the source of the capital projects.

The FY 2019 budget does not contain any capital projects being funded by a general obligation bond sale. The \$52.2 million that is in the FY 2019 budget for capital projects is being funded by general fund surplus dollars. In addition, the proposed bond resolution does not contain any specific language that authorizes the CFO to amend the FY 2019 budget to appropriate capital project expenditures being funded by the proceeds of the proposed UTGO bond sale.

In addition, when the Mayor presents his proposed FY 2020 budget to Council in March of 2019, that budget would need to contain his proposed capital projects that would also be funded by the proceeds of the UTGO bond sale for Council's consideration and deliberation.

It is LPD's opinion that the Administration, absent specific authorization given to it to amend the budget and appropriate the funds for the capital projects in the 2018 UTGO bond resolution approved by City Council⁹, is required to submit a budget amendment for City Council approval to appropriate the bond proceeds before expending them on the capital projects. **Furthermore, it is LPD's opinion, that it is necessary for the Administration to provide a budget amendment to Council subsequent to the sale of the bonds to appropriate the list of capital projects amounting to \$48.2 million for FY 2019 that are on the capital project list with proceeds from the proposed UTGO bond sale as the source of funding for those capital projects.**

⁸ The Budget Director is referencing Section 1002 from page 32 of the Bond Resolution that was before City Council for a vote last Tuesday, October 23, 2018 during Formal Session.

⁹ An example of specific authorization in a bond resolution is: Bond Resolution Series 2000 B&C UTGO Bonds Article II Section 204, dated November 22, 2000. "Amendments to 2000-2001 Budget. In order to facilitate the initiation by the Planning and Development Department of the housing stabilization program authorized by the voters, the Finance Director [Chief Financial Officer] is hereby authorized to amend the City's 2000-2001 Budget by appropriating an additional \$15,000,000 to the Planning and Development Department for capital improvements for housing stabilization projects."

The City of Detroit Charter, Article 8, Chapter 2, Section 8-207, gives the City Council authority over the City's Budget and requires the Council to adopt the City's Budget¹⁰. The City Council is required to approve and adopt the annual City budget and any amendments [changes] to it. This includes amending the budget for bond proceeds and any appropriations for capital projects funded by those proceeds occurring subsequent to the adoption of the annual budget.

Section 8-210, paragraph 1, of the Charter states: "If during the fiscal year the Mayor advises the City Council that there are available for appropriation revenues in excess of those estimated in the budget [such as through a new bond issuance], the City Council may make supplemental appropriations for the year up to the amount of the excess."

The City's past bond resolutions required City Council to appropriate bond proceeds to Finance projects. For example, one such bond resolution included an authorization for the Finance Director [Chief Financial Officer] to "allocate the proceeds of such Bonds to finance those Projects or portions thereof as she may determine, and to make such changes or cause such changes to be made as may become necessary and are permitted by law in the allocation of the amount of proceeds of such Bonds required for the respective purposes of the Projects within the limitations set forth above, the authorizations of the Prior Elections and **subject to previous or future appropriations of Council or both. Anything in this Resolution to the contrary notwithstanding, in no event shall proceeds of the Bonds be used to finance Projects in amounts which have not been appropriated by the Council [emphasis added].**"¹¹

The Bond Authorizing Resolution – UTGO Bonds, Series 2018, and Refunding Bonds, Article III, Section 301(b), "AUTHORIZATION; PLEDGE; SECURITY; DESIGNATIONS; REDEMPTION OF THE BONDS" of, states: " Each Authorized Officer is hereby authorized to allocate the proceeds of the UTGO Bonds to finance those projects or portions thereof as he may determine and to make such changes or cause such changes to be made in allocation of the amount of the proceeds of the UTGO Bonds required for the respective purposes of the Projects as may become necessary and are **permitted by law within the limitations of the authorizations of the Prior Elections and subject to previous or future appropriations of Council or both.[emphasis added]**"

The City's Charter Section 8-304 "Obligations to be Met by Subsequent Appropriations", states, "As permitted by law, the City may by resolution of the City Council:

1. Make contracts or make or authorize payments for capital improvements to be financed wholly or partly by the issuance of bonds; or
2. Make any contract or lease (including installment contracts, lease-purchase contracts, or other forms of deferred payment contracts for the acquisition of real property or capital equipment) providing for payments beyond the end of the fiscal year."

¹⁰ Section 8-207 of the Charter states, "After the public hearing, the City Council may adopt the budget with or without amendment."

¹¹ Bond Resolution for 1997 A&B UTGO Bonds dated October 28, 1997, Article III Section 301 (b).

The intent of Section 8-304 of the City's Charter is to allow the City to enter into multi-year contracts and issue bonds that cover multiple years when there was no multi-year budgets or budget authority to obligate funds. In 2012 when the Charter was written the City only budgeted for one fiscal year. The City is bound in the future by the contracts and bonds that City Council approves with terms and conditions occurring over one year. When the City does appropriate the expenditures for those contractual obligations it still must do so through appropriations approved by the City Council. The appropriations would have to allow for the covenants and requirements of those bonds and contracts. The obligations issued under those contracts and other contracts with obligations funded by bond proceeds were intended to be covered by subsequent appropriations authorized/adopted by City Council in the years that applied. This Charter requirement does not allow the Administration to contract nor appropriate funds without approval of the City Council.

We recommend that the City Charter be revised to clearly state the City Council's authority over the City's budget. In addition, we recommend that the City Charter be revised to clearly state that the Office of the Chief Financial Officer must obtain City Council approval to amend the City's budgeted appropriations for any capital projects funded with bond proceeds that are not included in the City's adopted budget.

Please let us know if we can be of any more assistance.