House Legislative Analysis Section

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LOCAL GOV'T. REIMBURSEMENT AGREEMENTS

House Bill 6187 as introduced
First Analysis (11-27-90)

Sponsor: Rep. Michael J. Griffin
Committee: Corporations & Finance

THE APPARENT PROBLEM:

Various acts regulate the way in which local governmental units, such as counties, cities, school districts, and others, may raise revenue to pay for services which the entity wishes or is required to provide. In many instances taxes or different types of assessments are levied to pay for a particular government function; or, sometimes, governments will use their bonding authority to raise revenue, especially when a long-term public works project is involved. A local government entity may turn to a financial institution for a "letter of credit" upon which the entity is allowed to draw for a set amount of money. This type of debt generally is less expensive than other debt instruments and is increasingly being used to finance such things as sewer repair, landfill closures, or the cleanup of contaminated sites — activities in which local governments have become more involved in recent years. Financial institutions will only pledge a letter of credit if the local government signs a "reimbursement agreement," which provides that the local government will pledge revenues that it receives from maintaining or operating the public project to pay off the letter of credit. Apparently, though, some people feel that the law is unclear about whether local governments have authority to make reimbursement agreements. Instead of amending every act that applies to local governmental units, it has been suggested that a new act be created to specifically allow all local governments to use reimbursement agreements.

THE CONTENT OF THE BILL:

The bill would create a new act to authorize any local government entity (i.e. city, township, village, county, school district, port district, and others) to enter into a "reimbursement agreement" to pay for or perform an obligation imposed on it by law or a contractual agreement. A reimbursement agreement could be made to support the issuance of a letter of credit, surety bond, or third-party guarantee, and to give a note or other evidence of debt to secure the government entity's obligation; such an agreement, however, would not be subject to the governmental unit's statutory, charter, or constitutional debt limitations. Any otherwise valid reimbursement agreement, note, or similar record of indebtedness entered into by a governmental unit before the bill's effective date would be validated.

A local government entity that entered into a reimbursement agreement could pledge its revenues and, if it had ad valorem taxing power, its full faith and credit limited tax general obligation to pay off the agreement's debt or obligation. Upon entering into such an agreement, a governmental unit could pledge the revenues of a public improvement or enterprise to pay for its debt obligations under the agreement, and could create a lien on those revenues. The lien would be a statutory lien and could be made subject to existing or future liens created to secure bonds or other debt instruments.

A governmental unit could also agree to fix rates or charges for those services offered by the public improvement or enterprise which were enough to allow it to:

- operate and maintain the improvement or enterprise;
- meet all other obligations incurred as a result of the improvement or enterprise; and
- pay its obligations under the reimbursement agreement and a related note of indebtedness.

FISCAL IMPLICATIONS:

According to the Department of Treasury, the bill would not affect state or local budget expenditures. (11-20-90)

ARGUMENTS:

For:

Local governments interested in raising relatively inexpensive capital quickly in order to finance certain public works projects have turned to letters of credit offered by financial institutions. These, in turn, require that the local govermental unit sign a "reimbursement agreement" which essentially pledges the revenue which the local government will receive from operating or maintaining the financed public improvement to pay off the letter of credit. Despite the fact that these financing arrangements are currently used, some people fear that laws regulating local governments do not explicitly authorize their use. The bill would create a new act that would apply to all local governmental units which would specifically allow reimbursement agreements to be used and would establish guidelines for their use.

Against:

The bill specifies that a reimbursement agreement would not be subject to the governmental unit's statutory, charter, or constitutional debt limitations. This provision could pose risks for both local governments and the state if entering into such agreements overextended a governmental unit's ability to pay off its debts at some later date. The bill should at least require approval of such a debt agreement by the Department of Treasury (which is now standard procedure before a local government can take on certain types of additional debt) before it can be entered into.

POSITIONS:

The Michigan Bankers Association supports the bill. (11-14-90)

Comerica Bank supports the bill. (11-19-90)

The Southeastern Oakland Resource Recovery Authority supports the bill. (11-16-90)

The Michigan Municipal League supports the concept of the bill. (11-14-90)

The Department of Treasury has not yet taken a position on the bill. (11-20-90)