SFA BILL ANALYSIS

Senate Fiscal Agency • Lansing, Michigan 48909 • (517) 373-5383

House Bill 5328 (as reported without amendment)
Sponsor: Representative William R. Keith
House Committee: Education
Senate Committee: Education and Mental Health

Date Completed: 2-16-90

RATIONALE

The School Bond Loan Program was instituted approximately 30 years ago in order to make it financially possible for every school district in the State to build school facilities. Under the program, the State provides loans to school districts for the payment of principal and interest on unlimited tax bonds that have been approved by the district's voters. Before a bond issue can go to the voters, however, a school district must obtain preliminary qualification of the bonds from the State Superintendent of Public Instruction. Public Act 108 of 1961 requires schools wishing to have bonds qualified for an election to file an application of preliminary qualification of bonds before the election. As part of the application, a district must submit a proposed maturity schedule of the bonds. That maturity schedule must meet certain criteria in the Act, such as the requirement that the amount of principal maturing in any calendar year not be less than the amount of principal maturing in any prior calendar year. While most districts use traditional financing techniques, such as the issuance of serial bonds, some districts wish to sell capital appreciation bonds, which are issued at a large discount and defer interest payments to a later date. These bonds, which are the same as zero coupon bonds, do not meet the Act's maturity schedule requirements for qualification. The Act provides, however, that regardless of the amount of principal maturing in any calendar year and regardless of the ratio of debt to valuation of the school district, the State Treasurer may authorize principal maturities in any amount if the Treasurer determines that it is financially beneficial to the State or school district. This authorization generally comes after voters have approved the bond proposal. Thus, school districts wishing to issue capital appreciation bonds first must prepare a bond issue that has a maturity schedule that meets the Act's requirements, submit these bonds for preliminary qualification, receive approval from the State Superintendent, hold an election, and finally, if the voters approve the bonds, request a variance of the maturity schedule from the State Treasurer. This procedure, some people contend, hinders school officials from being able to explain adequately to the voters the bonds' financing schedule. Some people believe that a school district should be permitted at the time of filing for a preliminary qualification of capital appreciation bonds--before the election--to request authorization from the State Treasurer for a variance from the statutory requirements relative to the bonds' maturity schedule.

CONTENT

The bill would amend Public Act 108 of 1961 to permit the State Treasurer, at the request of a school district, to authorize principal maturities in any amount as part of the preliminary qualification of a bond issue that requires an election.

MCL 388.954

FISCAL IMPACT

The bill would have virtually no fiscal impact on the State, which could save funds under certain circumstances due to a local district's deferral of interest payments. There would be an indeterminate fiscal impact on local school districts. Total interest paid could be increased or decreased depending upon a number of factors related to the repayment schedules of capital appreciation bonds when compared to most bond repayment schedules. However, each issuance and variance would have to be approved by the State Treasurer.

ARGUMENTS

Supporting Argument

If the bill were enacted, a school district filing for preliminary bond qualification at the same time could request from the State Treasurer a variance from having to meet certain maturity schedule criteria. Since a school district could make this process a part of the preliminary qualification procedure, the district would be in a position to explain the financing method to the electors before an election on the bond issue.

Supporting Argument

Capital appreciation bonds are similar to a savings bond. The buyer purchases the bond at a discount and pays a small initial sum that is less than the face value of the bond. At a specified date in the future, the bond matures and pays its full face value. Capital appreciation bonds minimize the immediate tax burden on the school district by deferring payment of the interest until a later date. These reduced initial costs of a capital appreciation bond may translate into a lower tax levy. A school district that used a traditional bond issue, for example, might have to ask voters to approve a millage request of three mills. By using a capital appreciation bond issue, however, the same district may have to seek approval of a millage request of only one mill for the same amount of revenue that would be generated under either financing technique.

Opposing Argument

Depending on how the local school district structured its payment plan, the issuance of capital appreciation bonds could increase the cost of borrowing due to initial low principal and delayed interest payments.

Response: While the bill would allow the State Treasurer to grant a variance in principal maturities at the same time a preliminary qualification of the bonds was issued, rather than after voters approved a bond issue as currently is provided in the Act, the bill would maintain the requirement that the Treasurer determine whether such a variance would be financially beneficial to the State or school district.

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