NORTH CAROLINA
DEPARTMENT OF STATE TREASURER

STATE TREASURER OF NORTH CAROLINA
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STATE AND LOCAL GOVERNMENT FINANCE DIVISION
AND THE LOCAL GOVERNMENT COMMISSION

GUIDELINES FOR COMPLIANCE WITH GENERAL OBLIGATION BOND BALLOT QUESTION REQUIREMENTS (G.S. 159-61(d), as amended)

BACKGROUND

Section 36.3.(a) of Session Law 2023-134 (HB 259) amended G.S. 159-61(d), which sets forth the form of the ballot question to be used for local government general obligation bond referenda. The purpose of this memorandum is to provide guidance to local government units in complying with the modified requirements in G.S. 159-61(d), specifically, the requirements of both clause (1) and clause (2) of G.S. 159-61(d), as amended.

IMPORTANT NOTICES

This memorandum provides guidelines to express the views of the staff of the Local Government Commission ("LGC") regarding compliance with the new provisions of G.S. 159-61(d). LGC staff developed these guidelines through analysis and discussion with Department of State Treasurer staff and state bond counsel and solicited input and review from the UNC School of Government and local government bond counsel throughout the state. This memorandum does not constitute legal or financial advice. Local government units are not required to utilize these guidelines and should consult with their bond counsels and financial advisors to ensure compliance with the requirements of G.S. 159-61(d).

North Carolina Administrative Code (20 NCAC 03 .0108) further describes the limitations of memoranda issued by the LGC:

> "(a) The Commission may from time to time issue memoranda, statements and publications for the guidance of local officials and other interested parties. These documents are intended to be explanatory in nature, and not intended to be binding on anyone. They are intended to set forth procedures, etc. which the Commission believes a prudent man would follow under the circumstances outlined in the document and be able to comply with the requirements of good accounting practice, state law and regulations, and any specified federal law and regulations. Care must be taken by each governmental unit that their own specific circumstances are not so different from the normal circumstances that other procedures should be used."

G.S. 159-61(d)

Section 36.3.(a) of Session Law 2023-134 (HB 259) amends G.S. 159-61(d), as follows:

"(d) The form of the question as stated on the ballot shall be in substantially the following words:
~~"Shall~~ "Additional property taxes may be levied on property located in (name of unit of local government) in an amount sufficient to pay the principal of and interest on bonds if approved by the following ballot question. Shall the order authorizing $______ bonds plus interest for (briefly stating the purpose) and providing that additional taxes may be levied in an amount sufficient to pay the principal of and interest on the bonds be ~~approved?~~ approved, in light of the following:

(1) The estimated cumulative cost over the life of the bond, using the highest interest rate charged for similar debt over the last (maximum bond issuance term), would be ($_____).
(2) The amount of property tax liability increase for each one hundred thousand dollars ($100,000) of property tax value to service the cumulative cost over the life of the bond provided above would be ($_____) per year.

[ ] YES
[ ] NO""

These amendments become effective on December 31, 2023, and apply to bond referenda conducted by local government units after that date.

These guidelines focus on the requirements of both clause (1) and clause (2) of G.S. 159-61(d), as amended and will (1) explain how LGC staff interprets the requirements of these provisions, (2) explain how LGC staff plans to assist local government units with complying with the requirements of these provisions, and (3) provide a level of uniform interpretation for local government units to use in complying with the requirements of these provisions.

SECTION 1: Clause (1)—Meaning of "Cumulative Cost"

The estimated **cumulative cost** over the life of the bond, using the highest interest rate charged for similar debt over the last (maximum bond issuance term), would be ($______).

There are several items of cost that could be included in the meaning of "cumulative cost," including (a) repayment of the principal amount borrowed, (b) interest cost, (c) issuance costs, and (d) administrative costs of carrying the debt. A reasonable interpretation might include or exclude some of these cost items. LGC staff believes the most reasonable interpretation is that "cumulative cost" is intended to refer to total debt service (principal and interest). The basis for this interpretation is as follows:

"Cumulative cost" is not defined in clause (1), the Session Law, or Chapter 159 of the General Statutes. "Cumulative cost," however, is again used in clause (2) of the ballot question: "The amount of property tax liability increase for each one hundred thousand dollars ($100,000) of property tax value to service the cumulative cost over the life of the bond provided above would be ($_______) per year."

A similar requirement for disclosure of property tax liability is found in G.S. 159-55.1, which requires a statement of disclosures from the finance officer of the local government unit, including "an estimate of the increase in property tax rate, if any, necessary to service the proposed debt. If no increase in property tax rate is estimated to be needed, a brief statement to the effect that the existing projected revenues are expected to be sufficient to pay the *principal and interest* [emphasis added] of the bonds."

LGC staff therefore concludes:

- The disclosure statement required by G.S. 159-55.1 intends (in part) to provide information about the estimated impact, if any, on the property tax rate related to repayment of the principal of and interest on the bonds.

- The new clause (2) of G.S. 159-61(d) requires a ballot question to include a similar disclosure related to the "property tax liability increase" to "service the cumulative cost over the life of the bond."

- The use of the term "cumulative cost" in clause (2) of G.S. 159-61(d) may be reasonably interpreted to mean principal and interest based on an assumed similarity of intent between G.S. 159-55.1 and 159-61(d).

- The use of the term "cumulative cost" in clause (1) of G.S. 159-61(d) may be reasonably interpreted to mean principal and interest to be consistent with the term's use in, and assumed desire for consistency with, clause (2) of G.S. 159-61(d).

In addition, the introductory sentences of G.S. 159-61(d) refer twice to the possibility of additional property taxes being "levied in an amount sufficient to pay the *principal of and interest on* [emphasis added] the bonds", which is consistent with this interpretation.

Issuance costs are typically paid from the proceeds of the bonds and are not an additional cost to the unit. As such, LGC staff believes that issuance costs should not be included in determining the estimated cumulative cost over the life of the bond to avoid double-counting. Also, while there are likely various other ongoing costs associated with the bond indebtedness (i.e., rating agency surveillance fees, rebate consultant fees, etc.) that typically would be paid outside of the bond proceeds as an additional cost, LGC staff believes these costs are more minor and incidental and are not what the drafters intended to be included within the meaning of "cumulative cost."

In preparing the ballot question, a local government unit may want to consider modifying the language to clarify the meaning of "cumulative cost" as principal and interest cost. For example: "The estimated cumulative cost over the life of the bond, using the highest interest rate charged for similar debt over the last (maximum bond issuance term), would be $_______[, consisting of the $________ principal amount of the bond plus $_______ of estimated interest]." Since the lead-in sentence to G.S. 159-61(d) states "the form of the question as stated on the ballot shall be in *substantially* [emphasis added] the following words," LGC staff believes there is leeway to modify the ballot question language in this manner to provide this clarity to the voters.

SECTION 2: Clause (1)—Meaning of "Over the Life of the Bond"

> The estimated cumulative cost **over the life of the bond**, using the highest interest rate charged for similar debt over the last (maximum bond issuance term), would be ($_____).

Because clause (1) provides that the estimated cumulative cost is an estimate, LGC staff believes it is reasonable and proper to make whatever assumptions the unit believes are consistent with anticipated issuance plans (subject to historical LGC requirements). In most cases for non-enterprise debt, LGC staff believes using an assumption that the bonds be amortized in annual installments on a level principal basis over a term of 20-years, with the first principal installment being made one year following the date of issuance, would be historically consistent and reasonable. For enterprise debt, if the unit expects to issue the bonds structured on a level debt-service basis as opposed to a level principal basis (which is typically permitted by the LGC for enterprise debt), then a modification should be made in deriving the interest cost amount to be set forth in the ballot question. Additionally, if the unit anticipates at the time of the bond referendum that a materially different debt amortization structure is expected to be used (i.e., amortize over a shorter period of time, etc.), then modifications necessary to reflect the anticipated structure would be reasonable.

SECTION 3: Clause (1)—Meaning of "Highest Interest Rate Charged for Similar Debt Over the Last (maximum bond issuance term)"

> The estimated cumulative cost over the life of the bond, using the **highest interest rate charged for similar debt over the last (maximum bond issuance term)**, would be ($_____).

In order to determine the "highest interest rate charged for similar debt over the last (maximum bond issuance term)," each component of the calculation (interest rate, similar debt, maximum bond issuance term) should be separately reviewed.

(a) *Interest Rate*

Typically bond issues are structured with multiple maturities with different coupon rates associated with each particular maturity. Sometimes particular maturities are sold at a premium (which would result in such maturity bearing a higher coupon rate) or sold at a discount (which would result in such maturity bearing a lower coupon rate). These various rates and prices are combined, resulting in overall interest rate or cost of borrowing. While there are various rate calculation methodologies (e.g., arbitrage yield, average coupon rate, true interest cost, effective interest cost), the "true interest cost" (TIC) rate is the rate historically used by the LGC as the basis for awarding bonds at competitive sale. It also is generally considered the true measure of the overall rate of borrowing, which takes into account original issue premium and discount. LGC staff therefore concludes that the TIC rate is the appropriate interest rate calculation methodology to be utilized for the purposes of disclosures and calculations required for clauses (1) and (2) of the ballot question.

(b) *Similar Debt*

Debt can be distinguished in multiple ways, including by nature of security, credit worthiness of issuer, tax treatment, nature of purchaser, or method of sale. For example, the highest rate charged for a triple A-rated issuer might be less than the highest rate charged for a single A-rated issuer. LGC staff concludes that for the purpose of disclosures and calculations required for clauses (1) and (2) of the ballot question, "similar debt" may be interpreted to mean debt issued by a North Carolina issuer on a competitive sale of tax-exempt, fixed rate, new money bonds with a 20-year amortization on a level principal basis (assuming the determination of the life of the bond as described in Section 2 above is consistent). LGC staff has determined not to differentiate rates charged based on the credit rating of the issuer due to the lack of available data related to ratings for bonds sold and the belief that such rate differentials would not be material due to the high credit quality of bonds issued. LGC staff believes this approach is reasonable and consistent with the requirements of the new statutory provisions.

(c) *Maximum Bond Issuance Term*

The maximum maturity of a bond issue is governed by the provisions of G.S. 159-122, which provide that "the last installment of each bond issue shall mature not later than the date of expiration of the period of usefulness of the capital project to be financed by the bond issue." The LGC, as required by regulation, has established the maximum period of usefulness for capital projects to be financed by bonds as 10 to 40 years, depending on the nature of the capital projects. Most capital projects financed with voted general obligation bonds have a maximum period of usefulness of at least 20 years, and many typically-financed capital projects have a maximum period of usefulness of 40 years. However, the usual practice of the LGC is to limit the maximum maturity of a general obligation bond issue to 20 years. Given this fact, and given the fact that bond issues are typically structured with a 20-year term, LGC staff has concluded that for the purposes of disclosures and calculations required for clauses (1) and (2), the use of a "maximum bond issuance term" of 20 years is reasonable and appropriate.

(d) *Highest Interest Rate Charged for Similar Debt Over the Last (maximum bond issuance term)*

Using the assumptions described above to determine interest rate, similar debt, and maximum bond issuance term, LGC staff will analyze available historic data associated with competitive public sales to identify the highest rate charged over the appropriate time period (see item (c) above), culling out any competitive sales that do not meet such criteria (e.g., taxable bond sales, refunding issues, sales with differing amortization structures, etc.). As noted above, LGC staff has determined not to differentiate rates charged based on the credit rating of the issuer. This rate will be published on the Department of State Treasurer's website and will be provided to units upon request. This rate will be monitored by LGC staff and will be updated when either (a) the rate falls outside the 20-year lookback window (at which time a new highest rate charged would be determined that falls within the 20-year lookback window), or (b) the TIC rate for a new bond issue sold competitively by the LGC exceeded the current rate being used, in which instance such rate would become the highest rate charged until that rate is either surpassed or an additional 20-year time frame passes.

Based on the foregoing assumptions, the local government unit would work with its financial advisor and bond counsel to calculate the estimated interest cost to be included in the "cumulative cost" in clauses (1) and (2) of the ballot question. Note that this estimated amount of interest may be different than the "estimate of the total amount of interest that will be paid on the bonds over the expected term of the bonds" included in the statement of disclosures required by G.S. 159-55.1 (which often utilizes a reasonably expected interest rate based on current market conditions rather than the highest interest rate over the past 20 years). This difference is due to the different interest calculation requirements in the two statutes. No change was made to G.S. 159-55.1 in connection with the new language requirements for the ballot question. The local government unit, with input from its financial advisor and bond counsel, may choose to use the highest interest rate described above in preparing the statement of disclosures required by G.S. 159-55.1. If the interest on the proposed bonds is expected to be subject to federal income taxation, then the highest rate for a taxable bond issued during the proposed term should be used, and the LGC staff will work with the unit to determine such rate.

SECTION 4: Clause (2)—Meaning of "Amount of Property Tax Liability Increase"

> The **amount of property tax liability increase** for each one hundred thousand dollars ($100,000) of property tax value to service the cumulative cost over the life of the bond provided above would be ($_____) per year.

Although clause (1) expressly references an "estimated cumulative cost," clause (2) does not expressly state that the property tax liability increase is an estimated amount. Nonetheless, at the time of a bond referendum, it is reasonable to interpret "the amount" in clause (2) as being an estimate. The tax rate that is needed to service the debt depends on multiple factors that may change over time, such as interest rates, term of the bond issue, changes in property tax values, change in property tax base due to annexations, natural growth or loss of major taxpayers, political pressures, increases and decreases in other indebtedness, etc. For purposes of providing this information, LGC staff believes it is appropriate for the unit to make its best judgment based on all facts and circumstances and its reasonable assumptions as to the debt service requirements for the proposed bonds. In preparing the ballot question, a unit may want to consider modifying the language to insert a word such as "estimated," "expected," or "anticipated" before the word "amount" to clarify that such increase is not definitive and is subject to change. For example: "The [estimated / expected / anticipated] amount of property tax liability increase . . . ."

In addition, if no property tax rate increase is expected to be necessary to pay debt service on the proposed bonds, LGC staff believes it would be appropriate to modify clause (2) to reflect the same. Sample language for this might be similar to the following: "No property tax liability increase is expected to be required to service the cumulative debt service cost over the life of the bond." LGC staff believes this is consistent with the treatment for estimating property tax rate increases in the statement of disclosures required by G.S. 159-55.1. Again, since the lead-in sentence to G.S. 159-61(d) states "the form of the question as stated on the ballot shall be in *substantially* [emphasis added] the following words," LGC staff believes there is leeway to modify the ballot question language as described above to provide clarity to the voters.

SECTION 5: Clause (2)—Meaning of "Cumulative Cost"

> The amount of property tax liability increase for each one hundred thousand dollars ($100,000) of property tax value to service the **cumulative cost** over the life of the bond provided above would be ($_____) per year.

As discussed in Section 1 above, LGC staff believes the most reasonable interpretation of "cumulative cost" is total debt service (principal and interest).

SECTION 6: Clause (2)—Meaning of "For Each One Hundred Thousand Dollars of Property Tax Value"

> The amount of property tax liability increase **for each one hundred thousand dollars ($100,000) of property tax value** to service the cumulative cost over the life of the bond provided above would be ($_____) per year.

It is important to note that the property tax liability increase that must be included in the ballot question is stated as an increase per $100,000 of property tax value. This is different from the way in which the increase in property tax must be disclosed in G.S. 159-55.1(b), which is based on the more customary measure of amount per $100 assessed valuation. A one-cent tax increase per $100 of assessed valuation equals a $10 increase per $100,000 of assessed valuation:

$$\$0.01/\$100 = (\$0.01 \text{ x } 1{,}000)/(\$100 \text{ x } 1{,}000) = \$10/\$100{,}000$$

For example, a penny tax rate increase for each $100 of property tax value on a property valued at $300,000 would mean a total tax increase of $30 ($300,000/$100 x $0.01). That same tax liability increase of $30 on a property valued at $300,000 would be stated as $10 for each $100,000 of property tax value ($300,000/$100,000 x $10).

CONCLUSION

This memorandum has been issued by the staff of the LGC to assist local government units in complying with the modifications to G.S. 159-61(d) enacted by Section 36.3.(a) of Session Law 2023-134 (HB 259). The guidance expressed here does not constitute legal advice, and its use and limitations are subject to North Carolina Administrative Code (20 NCAC 03 .0108). Units should consult their bond counsel to ensure the requirements of G.S. 159-61(d), and all applicable laws, are met.