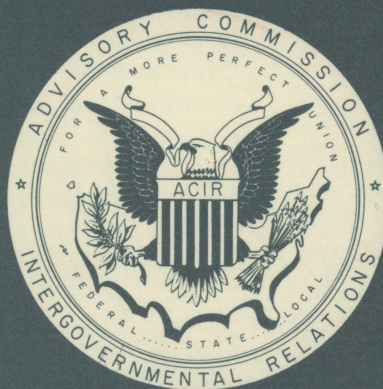


AN INFORMATION REPORT

State Technical Assistance to Local Debt Management



ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS
JANUARY 1965
M - 26

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PREFACE

In its report on State Constitutional and Statutory Restrictions on Local Government Debt, this Commission recommended that:

States make available technical and advisory assistance to local governments with regard to the issuance of long-term debt; and that the State agency responsible for this function be empowered to prescribe the minimum content of official statements prescribed by local governments in connection with their issuance of long-term debt, in order to provide prospective investors with data needed to evaluate the security offerings.

The Commission believes that technical and advisory assistance in the flotation of long-term debt would be especially helpful to relatively small local governments. These governments issue bonds less frequently than major units and are often less well equipped, through their own financial staff and locally available advisers, to deal with the complexities of long-term borrowing. Local government would benefit materially from the information and advice that could be supplied by a State office with a continuing responsibility for providing such service.

This informational report on the potential scope of technical assistance to local debt management is intended to encourage and facilitate the activity of State governments in this field.

Dr. Wylie Kilpatrick, Research Professor at the College of Business Administration, University of Florida, assembled the information and prepared the initial draft for this report, under contract with the Commission. Jacob M. Jaffe, of the Commission staff, supplemented these materials and prepared the report for publication.

Wm. G. Colman,
Executive Director

L. L. Ecker-Racz,
Assistant Director

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Chapter 1

THE CASE FOR STATE TECHNICAL ASSISTANCE

Summary of Findings

States have an inescapable interest in and concern with the quality of the debt management practices of their local governments. Each community's practice is a matter of statewide concern because a blemish on its credit standing, perhaps on only a single bond issue, could affect the money market's judgment of local bond issues in that State. The dramatic increase in local borrowing since the end of World War II also underscores the need for State concern with local debt practices.

A State technical assistance program, as outlined in this report, is designed to accomplish several objectives:

1. Local governments would be able to estimate more accurately the limits of their debt-servicing capacity and thereby prevent fiscal strains, correct fiscal imbalance, and reduce the risk of default.
2. Local governments would also be able to reduce their debt costs because an assistance program would tend to upgrade the quality of their debt offerings and intensify competition for them.
3. State policy makers would be in a better position to overhaul their present system of debt controls because the requisite information would be available to them. 1/

The basic technical assistance program described in detail in chapter 2 is designed to help local governments in debt management and to maximize the amount of information that can be made available to investors for evaluating local government debt offerings, while at the same time holding to an irreducible minimum the amount of

1/ For a description of basic recommendations see the policy proposals made by the Advisory Commission on Intergovernmental Relations set forth in Appendix A.

State involvement in local fiscal management. To accomplish these objectives the basic or minimum assistance plan should contain the following key elements:

1. Simplification and modernization of the debt laws;
2. Development and maintenance of a State file on local debt and related data;
3. Dissemination of data on local government finances;
4. Preparation of standards for official statements on local debt offerings; and
5. Development of an educational program for local finance officials.

While the basic plan for State technical assistance to local debt management is considered the minimum level of State involvement, some States may wish to take two additional steps in order to help local governments improve the quality of their debt offerings. As analyzed in detail in chapter 3, these two "high option" forms of technical assistance are:

1. Advisory review of both the legal and fiscal aspects of proposed local bond issues; and
2. Optional State sale of local bonds.

These supplemental forms of technical assistance should prove of special benefit to (a) local communities in depressed areas with particular need for the additional assistance that can be provided by a State advisory review service and (b) small communities that do not enjoy ready access to the money market.

It must be emphasized that neither of these proposed activities involves coercion on the part of the State. Thus, while a State agency reviewing the proposed bond issue may feel strongly that the project is ill-conceived and possibly unnecessary or that the issuing government may be borrowing beyond its fiscal capacity, it is not given the authority to forbid the issue. There is no doubt, however, that a strongly negative report is likely to have a deterrent effect on the borrowing plans of the local government that

has come voluntarily to the State for advice. 1/

Because an understanding of the essential characteristics of the bond market is essential to the formulation of an effective State technical assistance program, this report describes in some detail three salient market characteristics: (a) primary factors responsible for the steady rise in local debt costs; (b) the difficulties experienced, particularly by small governments, in coping with the complexities of the bond market; and (c) the general ineffectiveness of the existing State systems for controlling local governmental debt offerings.

THE GROWTH OF LOCAL GOVERNMENT INDEBTEDNESS AND INTEREST COST

The provision of domestic governmental services in this country is primarily the responsibility of the States and their localities, and almost half of all expenditures for civilian government (excluding defense, expenditures for past wars, etc.) occurs at the local level. 2/ As the demand for governmental services such as schools, highways, water supply, and sewage disposal increases, so does the demand for public facilities, financed in large part with borrowed funds.

Recent Trends in Debt Outstanding and Issued

Local government indebtedness is now at an all-time high, near the \$70 billion mark by the end of last year (1964). At the close of their fiscal years ending in 1963, local governments had a gross debt of \$64.3 billion, almost three times the \$23.2 billion

1/ In the case of local industrial development bonds, the Advisory Commission has recognized one exception to its general position that State administrative involvement be essentially advisory in character. In its report, Industrial Development Bond Financing, the Commission pointed out the possible abuses that can flow from this type of public subsidy and recommended that the States impose several safeguards, including the requirement that all such proposals be submitted for State approval.

2/ Advisory Commission on Intergovernmental Relations, Tax Overlapping in the United States (M-23), July 1964, p. 6.

outstanding in 1952 (table 1). Over \$60 billion of this was long-term indebtedness.

The annual gross volume of new bond issues (State and local) has also increased at a dramatic rate - rising from less than \$4 billion in 1952 to more than \$10 billion in 1963 and 1964. Three-fourths of this total represented local long-term borrowing (table 1); one-fourth State borrowing.

Not only has the total local debt been increasing, but its character has been changing. While the amount of local full faith and credit debt outstanding in 1963 was a little more than double the 1952 total, nonguaranteed debt (primarily "revenue" bonds) rose to almost 4½ times the 1952 figure. ^{1/} In 1952, nonguaranteed debt represented only one-fifth of all local long-term debt outstanding; by 1963 it had reached one-third of the total.

There are a number of reasons for the increase in revenue bond financing. Revenue bonds are generally outside constitutional and statutory limitations and in many States need not be submitted to the electorate for approval. In some States, special authorities have been organized to finance the construction of school buildings with revenue bonds, pledging rentals paid by the operating school districts to the servicing of the bonds. The rapid urbanization and suburbanization of the population has generated unprecedented demands for additional and expanded water supply and sewer systems. Current activities in the field of public mass transportation, spurred by a recently enacted Federal aid program, will undoubtedly accelerate the pace of revenue bond financing in the next few years. Although, as has been indicated, much of the nonguaranteed debt has been issued to avoid debt limitations and bond elections, there is wide acceptance of the theory that the debt of a revenue-producing facility should be serviced from the fees paid by its users. Local officials often justify incurring the extra costs connected with the issuance of revenue bonds in order to conserve their tax base for servicing future issues of general obligation bonds.

^{1/} "Full faith and credit debt" is defined by the Bureau of the Census as long-term debt for which the credit of the government, implying the power of taxation, is unconditionally pledged. "Nonguaranteed debt" is defined as debt payable solely from pledged specific sources.

TABLE 1. - LOCAL GOVERNMENT DEBT, BY GOVERNMENTAL SECTOR AND BY TYPE,
 SELECTED YEARS, 1952 - 1963
 (dollar amounts in millions)

Item	1963	1957	1952	Percentage increase 1952 - 1963
Total debt outstanding end of fiscal year	\$64,276	\$39,301	\$23,226	177
By governmental sector:				
General	50,310	30,058	n.a.	n.a.
Utility	13,966	9,243	n.a.	n.a.
By type:				
Long-term	60,399	37,323	22,080	174
Full faith and credit	40,046	26,087	17,510	129
Nonguaranteed	20,353	11,236	4,571	345
As percent of long- term debt	33.7	30.1	20.7	x x
Short-term	3,876	1,979	1,146	238
Long-term debt issued during fiscal year	7,861	5,323	2,714	190
Interest on total debt	1,932	1,025	580	233
Interest on general debt	1,478	755	408	262
As % of property tax revenue	7.6	6.1	4.9	x x
As % of general revenue	3.6	3.0	2.4	x x

n.a. - data not available.

Source: U. S. Bureau of the Census, Historical Statistics on Govern-
 mental Finances and Employment, 1962 Census of Governments,
 Vol. VI, No. 4; Compendium of Government Finances, 1962
 Census of Governments, Vol. IV, No. 4; and Governmental
Finances (Annual).

Recent Trends in Interest Expenditure

The growth in the outstanding debt of local governments has naturally been accompanied by an increase in interest payments. Actually, interest expenditure has risen at a considerably faster rate than total debt (table 1). While gross debt increased 177 percent between 1952 and 1963, total interest (on utility and general debt) rose 233 percent, from \$580 million to almost \$2 billion; and, interest on general debt rose even faster -- 262 percent. 1/ This rapid increase in interest on debt incurred for general government purposes is significant when compared with the growth of property taxes and other general revenue from which this interest is paid. In 1952, local expenditure for interest on general debt was 2.4 percent of total general revenue; by 1963 it amounted to 3.6 percent.

Effect of shift toward nonguaranteed debt -- The growing reliance on revenue bond financing is one of the developments responsible for the fact that interest costs outpaced the growth in total debt. Revenue bonds have been considered to involve more of a risk than general obligation bonds and investors have demanded higher yields from them than from general obligation bonds. The amount of yield differential between revenue bonds and general obligation bonds varies, depending upon market conditions, the nature of the enterprise to be financed, and the terms of the bond issue. Thus, revenue bonds issued by a newly established public authority to finance a toll road would require a substantially higher yield to attract investors than would State general obligation bonds backed by gasoline taxes and Federal aid. In the mid-1950's, when toll road financing constituted a sizeable portion of the "municipal" bond market, the yield differential between revenue and general obligation bonds was estimated at from 3/4 of 1 percent to 1½ percent. 2/ The differential has declined significantly in recent years, and a recent estimate indicated a much smaller difference in the yield -- about 1/8 of 1 percentage

1/ "General" debt is debt other than that incurred for water supply, gas, electric, and transit systems owned and operated by local governments.

2/ Roland I. Robinson, Post War Market for State and Local Government Securities, Princeton University Press (Princeton: 1960), p. 211.

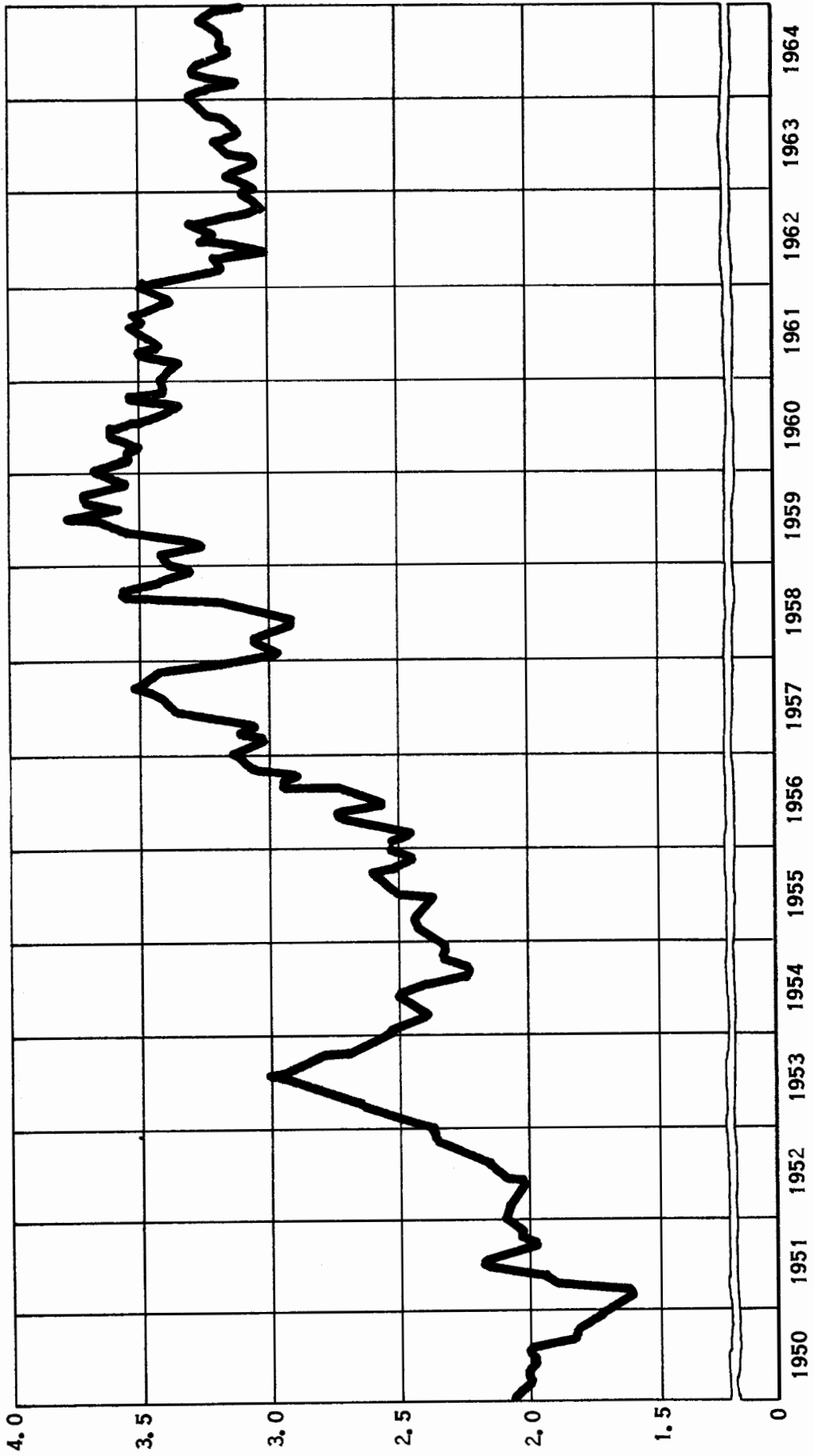
point. 1/ A more reasonable estimate is between these extremes, perhaps 1/3 of a percentage point, from which variations would be expected by reason of the bond market and the character of the borrowing government. There is also a small differential in the spread (the underwriter's fee for handling a bond issue -- a factor entering into the pricing) as between general obligations and revenue bonds. 2/

Effect of rising interest rates -- The general increase in interest rates has also contributed to the steeper rise in interest costs than in outstanding debt. As the accompanying chart shows, the Bond Buyer's index of yield (based on the yield of 20 State and local bonds) rose from a low of 1.7 percent in 1951 to a high of 3.8 percent in mid-1959, with considerable fluctuation in between. By mid-1962 the index fell to 3.0 percent, and the yield has been fairly stable since then, at about 3.2 percent.

Since the end of World War II, when yields (and therefore the price -- or the interest rate -- paid by local governments for borrowed money) were extremely low, the trend has been generally upward. The interest rate on local government bonds varies with changes in the bond and money markets. As the volume of local government bond issues (the supply) has increased, the required yield has also increased in order to attract more buyers. Fluctuations in the supply of available investment funds also affect the prices paid for "municipals." Thus, when there is a plentiful supply of money available to commercial banks (for example, when the demand for business loans drops) they enter the municipal bond market, offering to accept lower yields. When the banks face a large demand for loans, or the available money supply is tightened for other reasons, they liquidate their "municipals" and yield offers are raised to attract other investors.

1/ Chester W. Laing, Statement to Taxation and Finance Committee, National Association of Counties (mimeographed), August 9, 1964, p. 6.

2/ "Municipal Bond Underwriting Compensation," I.B.A. Statistical Bulletin, Investment Bankers Association of America, (Washington, D. C.: June 1964), Occasional Paper No. 7.



The Bond Buyer's Index of the Municipal Bond Market, 1950 - 1964

THE STATE'S CONCERN WITH SMALL GOVERNMENT BORROWING

The planning and financing of a capital improvement program are extremely technical processes, and, as an observer wrote recently:

... the procedures involved (in the authorization, issuance, sale, and delivery of municipal bond issues)...are becoming more and more complicated. 1/

... no outline of procedure...which purports to instruct in the intricacies of the issuance and sale of municipal bonds should ever be treated as a do-it-yourself kit. 2/

Except for the large local governments, which are in the bond market almost continuously, the average community cannot afford to have on its payroll the technically competent legal and financial personnel needed to carry a bond issue through the intricacies called for by the statutes and by the bond market. The municipal finance officers of many small communities are fairly well versed in the details of budgeting, record keeping, and financial reporting, but their communities enter the money market too infrequently for them to develop more than a nodding acquaintance with the financial labyrinth through which a bond issue must be guided to fruition. Even such seemingly simple decisions as the time an issue should be offered, the maturity schedule, and whether or not to include a call feature, contain pitfalls for the uninitiated.

Extent of Borrowing by Small Governments

Much of the indebtedness of local governments is owed by relatively small localities. At the end of their 1962 fiscal years all municipalities, counties, and school districts had outstanding debt of \$46 billion (table 2), and the total was approaching \$50 billion by the end of 1963. Fully one-third of the 1962 indebtedness, or \$15.4 billion, was attributed to numerous small governments, and those governments paid out about a half billion dollars in interest.

1/ W. E. Tinsley, Getting the Best Price for Your Bonds. Municipal Finance Officers Association, Special Bulletin 1963C (Chicago: September 16, 1963), p. 1.

2/ Ibid, p. 2.

TABLE 2. - DEBT OUTSTANDING AND INTEREST EXPENDITURE FOR LARGE AND SMALL MUNICIPALITIES,
COUNTIES, AND SCHOOL DISTRICTS, 1962

(dollar amounts in millions)

	Total		Municipalities			Counties			School districts		
	Debt	Interest	No.	Debt	Interest	No.	Debt	Interest	No.	Debt	Interest
Large governments <u>1/</u>	\$30,733	\$ 907	310	\$19,840	\$575 <u>2/</u>	560	\$4,476	\$131	795	\$ 6,417 <u>2/</u>	\$201 <u>2/</u>
Small governments <u>1/</u>	15,436	496	17,690	7,017	229 <u>2/</u>	2,483	905	28	33,883	7,514 <u>2/</u>	239 <u>2/</u>
Total	46,169	1,403	18,000	26,857	804	3,043	5,381	159	34,678	13,931	440
Small governments as percent of total	33.4	35.4	98.3	26.1	28.5	81.6	16.8	17.6	97.7	53.9	54.3

1/ The cutoffs are: for municipalities and counties, population of 50,000; and for school districts, enrollment of 6,000.

2/ Estimated.

Source: U. S. Bureau of the Census: Finances of Municipalities and Township Governments, 1962 Census of Governments, Vol. IV, No. 3; Finances of County Governments, 1962 Census of Governments, Vol. IV, No. 2; and Finances of School Districts, 1962 Census of Governments, Vol. IV, No. 1.

Of the 34,678 school districts in the United States in 1962, 33,883 enrolled fewer than 6,000 pupils each and owed more than half of the \$13.9 billion school district debt. Municipalities with fewer than 50,000 inhabitants each numbered 17,690, and they accounted for over one-fourth of the total municipal indebtedness. And, some 2,500 small counties (those with fewer than 50,000 inhabitants) owed one-sixth of all county debt.

Complexities of the Bond Market

The finance officers of those small local governments need help when their governing bodies and electorate decide to borrow money in order to build a new school building, a city hall, or a county courthouse. The following chapters will describe some of the kinds of technical assistance States could provide, although only a few do so now.

It should be noted that professional legal and financial services are made available to governmental borrowers by the investment market itself. Some investment banking firms and the municipal bond departments of a few commercial banks have published excellent bulletins on the mechanics of a municipal bond issue. In addition, many such firms actively solicit the opportunity to provide local governments with professional advice and assistance in all phases of a bond issue. While these services are useful to the localities, it is the financial community's aim to put together a marketable bond package -- one that will attract investors.

Local governments generally hire the services of private bond counsel to help them with the legal problems connected with bond issues. It is almost standard practice for underwriters to bid subject to the unqualified approving legal opinion of a recognized bond attorney, even in those States where local bond issues are validated by the attorney general or some other State official.

The bond rating services -- Moody's Investors Service, Standard and Poor's, and one or two others -- help local governments indirectly by compiling and evaluating the financial data for the purpose of establishing credit ratings. 1/ The credit rating of a local

1/ Since credit ratings are not developed for governments that issue small amounts of debt, this kind of service is, of course, not available to many small governments. As a general rule, Moody's rates only the bonds of issuers with debt of \$600,000 or more, and Standard and Poor's rates only governments with debt of at least \$1 million.

community is influenced by the adequacy of municipal financial records, or the lack thereof, and the ability of local governments to present a clear and comprehensive picture of their finances. Furthermore, the rating attached to a particular bond issue depends upon the nature of the facility it is to finance and the security backing it. The rating services and the Investment Bankers Association provide guidelines as to the kinds of information needed by the bond buyers in making their investment decisions.

In addition, the national organizations of the local governments themselves -- the Municipal Finance Officers Association, the National League of Cities, 1/ and the National Association of Counties (together with their State counterparts) -- offer an array of financial services to their member municipalities in the form of conferences, seminars, and technical publications. The Michigan Municipal League provides a complete financial consulting service in connection with bond issues, on a fee basis, to members and non-members alike, similar to the services provided by private bond consultants.

To the uninitiated, the municipal bond market is a highly technical mechanism whose operations are all but unfathomable. A complex network of interrelationships has developed between municipal bond dealers (some 800 investment bankers and about 150 commercial banks) and the governmental borrowers; among the traders themselves; and between the traders and the ultimate investors. A complete description and explanation of the municipal bond market cannot be undertaken here. 2/ However, a few of the problem areas in which State technical assistance can help reduce the cost of local government borrowing are described below.

1/ Formerly the American Municipal Association.

2/ A brief, rather non-technical, description can be found in Investment Bankers Association of America, Fundamentals of Municipal Bonds (Washington, D. C.: January 1963), third edition. The rating services and a number of investment banking firms have also published descriptive books and pamphlets on the subject. A volume that delves more deeply into the technicalities and the economics of the municipal bond market is Roland I. Robinson, op. cit.

The purchasers of local government bonds -- Under the usual marketing conditions for sizeable bond issues, a bond offering is purchased initially, on the basis of the lowest bid (i.e., the lowest net interest cost to the issuer), by an underwriter syndicate consisting of a group of bond dealers. Once the bid has been accepted by the borrowing government, the bonds are reoffered by the underwriter on a "when issued" basis and the members of the underwriting syndicate sell the bonds to the ultimate investors. The offerings of small governments are often taken up by local banks. Such banks, which hold the deposits of local governments, generally feel duty-bound to see that their local governments "get at least one decent bid." 1/ In many instances very small bond issues (as well as very large ones) are negotiated, rather than let out for bids.

The tax-exempt status of State and local government bonds, among other features, such as security and marketability, makes them attractive investments for the moderate- and high-income groups. It is not surprising, then, that a considerable share of all "municipals" is held by individuals.

Table 3 shows the distribution of State and local government securities among various classes of private investors. Private individuals and commercial banks have held the largest share throughout the period 1952-1963 -- from a little less than three-fourths to over four-fifths of the total. Most of the remainder is held by fire, casualty, and life insurance companies. Among the minor private purchasers of State and local government securities are savings and loan associations, mutual savings banks, fraternal organizations, and corporate pension funds.

The proportion of "municipals" held by commercial banks has ranged more widely than for other types of investors because of the tendency for the banks to move in and out of the bond market according to the vacillations of the money market.

The investors' need for information -- To make intelligent decisions concerning the kinds of municipal bonds they will purchase and the price they will offer for them, bond dealers and the ultimate investors need information concerning the governments whose offerings they buy. They must have ready access to information on

1/ Roland I. Robinson, op. cit., p. 104.

TABLE 3. - ESTIMATED PRIVATE OWNERSHIP OF STATE AND LOCAL
GOVERNMENT SECURITIES OUTSTANDING,
June 30, 1952 - 1963

Year	Total	Individ- uals <u>1/</u>	Commercial banks	Insurance companies	Corpora- tions <u>2/</u>	Miscel- laneous investors <u>3/</u>
Amount (in billions of dollars)						
1952	24.6	10.5	9.9	2.8	.6	.8
1953	27.4	11.6	10.6	3.5	.7	1.0
1954	32.5	13.8	12.0	4.6	.9	1.2
1955	37.6	16.4	12.8	5.8	1.1	1.5
1956	42.1	19.5	13.0	6.6	1.4	1.6
1957	46.0	22.0	13.4	7.4	1.5	1.7
1958	50.1	22.8	15.8	8.2	1.5	1.8
1959	54.8	24.6	17.0	9.5	1.7	2.0
1960	59.0	27.2	16.8	10.9	1.9	2.2
1961	63.9	28.3	18.8	12.3	2.2	2.3
1962	72.4	30.7	23.2	13.4	2.7	2.4
1963	79.0	31.7	27.9	14.1	3.0	2.3
Percent distribution						
1952	100.0	42.7	40.2	11.4	2.4	3.3
1953	100.0	42.3	38.7	12.8	2.6	3.6
1954	100.0	42.5	36.9	14.2	2.8	3.7
1955	100.0	43.6	34.0	15.4	2.9	4.0
1956	100.0	46.3	30.9	15.7	3.3	3.8
1957	100.0	47.8	29.1	16.1	3.3	3.7
1958	100.0	45.5	31.5	16.4	3.0	3.6
1959	100.0	44.9	31.0	17.3	3.1	3.6
1960	100.0	46.1	28.5	18.5	3.2	3.7
1961	100.0	44.3	29.4	19.2	3.4	3.6
1962	100.0	42.4	32.0	18.5	3.7	3.3
1963	100.0	40.1	35.3	17.8	3.8	2.9

1/ Includes partnerships and personal trust accounts.

2/ Exclusive of banks and insurance companies.

3/ Includes mutual savings banks, savings and loan associations, non-profit associations, corporate pension trust funds, dealers and brokers, and investments of foreign balances and international accounts in this country.

Source: U. S. Treasury Department, Annual Reports of the Secretary.

the local government's finances, its structure, and its social and economic base.

Investors depend heavily upon the credit ratings placed upon individual bond issues by Moody's, Standard and Poor's and the other rating firms. The rating firms, in turn, depend upon information they obtain from the local governments themselves, from the States, and from other sources. Where meaningful data cannot be obtained, a rating may not be given, or, if given, it may be lower than the local government deserves.

There is a distinct correlation between the price of a municipal bond and the credit rating of the borrower. Robinson calculated, on the basis of 1955 yields, that the yield differential between a high grade bond (Moody's Aaa) and one of intermediate grade (Baa) would have allowed an investor to build up a reserve of \$260 over a 20-year period on a \$1,000 bond by purchasing a Baa rated bond rather than an Aaa rated bond. 1/ Even the differential between Aa and Aaa rated bonds of like maturity ranges from 10 to 20 basis points. 2/

Volatility of the municipal bond market -- The municipal bond market has been described recently as "highly volatile and dynamic" -- surprisingly so, in view of its relative price stability in the past two or three years. 3/ As the chart on page 8 indicates, the Bond Buyer's index of municipal bond yields was at a low of about 1.7 percent early in 1951, reached one peak at about 3.1 percent in mid-1953, dropped to about 2.3 percent in mid-1954, moved up to 3.6 percent by 1957, declined to about 2.9 percent in 1958, hit a high of about 3.8 percent in mid-1959 and has settled down to an average of about 3.2 percent since 1962.

1/ Roland I. Robinson, op. cit., p. 177.

2/ A "basis point" is one-hundredth of one percentage point in the expression of yield; i.e., a change of yield from 3.16 to 3.12 is referred to as a drop of four basis points. It should be noted that a difference of 25 basis points on an issue of \$1,000,000 bonds maturing serially out to 25 years means an extra interest expense of \$40,275 over the life of the issue.

3/ Sidney Homer, The Changing Market for Municipal Bonds, Municipal Finance Officers Association, November 1, 1964, Special Bulletin 1964A.

Homer's analysis goes back to 1900, when the yield of a prime municipal bond was about the same as it is today -- a little over 3 percent -- but without the advantage of the income tax exemption. The yield rose steadily to about 5 percent in 1920, even after imposition of the Federal income tax, but then turned downward, falling rapidly during the depression years, and even more rapidly when steep World War II income tax rates were put into effect. By 1945 the yield was at an all-time low of about 1/2 of 1 percent. 1/

Even in recent years, when the yields have been rather steady, one can detect significant month-to-month, and even week-to-week variations. Looking at yearly highs and lows since 1958, we find the following results (based on the Bond Buyer's index of 20 bonds):

Year	High yield %	Low yield %	Number of basis points differential
1964	3.32	3.12	19
1963	3.31	3.01	30
1962	3.37	2.98	39
1961	3.55	3.26	29
1960	3.78	3.27	51
1959	3.81	3.26	55
1958	3.59	2.85	74

1/ Ibid, p. 3.

The dynamic nature of the municipal bond market is a significant factor that the knowledgeable finance officer can put to good advantage. As has been noted, there have been periods when even short-term fluctuations were wide, so that savings in interest costs could be realized by timing bond offerings to take advantage of these fluctuations. However, local finance officers do not always have the leeway to do this, considering the political pressures that may be exerted to get a project underway once a bond issue has been approved.

Bidding practices -- As has been mentioned, bonds are usually sold by local governments, generally to underwriting syndicates, on the basis of competitive bidding. As in the case of other kinds of governmental purchasing, awards are made to the lowest bidder; that is, to the syndicate that offers the lowest net interest cost for the bond issue.

Selection of the lowest bidder is not as simple as it may appear, although most awards are made merely on the basis of straight net interest cost. A recent Bond Buyer article points up some of the complexities of bidding. 1/

Bids are made in terms of coupon rates -- that is, the rate of interest that applies to each individual bond or to a series of bonds. Sometimes, a series of coupon rates is quoted, with high rates on the early maturities and extremely low rates, at times ranging from 1 percent to 1/10 of one percent, on the last few maturities. 2/ Any number of variations can be used, and the net interest cost can be computed for each bid by applying certain formulas. Ryan points out that when this type of "trick" bid is submitted the one that yields the lowest net interest cost is not necessarily the bid most favorable to the issuer. In these circumstances the borrower should take into account that the heaviest interest payments will have to be made in the earliest years of the maturity schedule, and that if this money were invested in those years, rather than paid out as interest, the borrower might be better off in the long run.

1/ William J. Ryan, "Trick Coupons Lower Net Interest Costs but Complicate Issuer's Fiscal Affairs," The Bond Buyer, Special Municipal Conference Issue, October 7, 1964, p. 15.

2/ Referred to by Ryan as the "high-low couponing technique."

This "trick" or "gimmick" bid is not submitted to befuddle the borrower. Underwriters have to buy marketable bonds, and they try to obtain the kinds of bonds their customers (investors) demand. There appears to be a demand for very high coupon-rate short-term bonds, at a premium, by some investors, and for very low coupon-rate long-term bonds, purchased at a deep discount, by others. The advantages of deep discount bonds to certain kinds of investors, such as insurance companies and pension funds, have been pointed up in a recent Bond Buyer article. 1/

Local finance officers must understand how to evaluate alternative kinds of bids. A good State technical assistance program can help them do so.

The matter of attracting bids should be mentioned here. Obviously, the more competition there is for a local government's offerings, the better the offer that can be obtained. The current debate between the commercial banks and the investment bankers concerning the underwriting of revenue bonds points up this issue. Commercial banks are authorized to underwrite general obligation bonds, but not revenue bonds. A number of bills have been introduced in the Congress that would authorize commercial banks to participate in revenue bond underwriting, and extensive hearings were held during 1963. 2/ The commercial banks contend that their participation would intensify competition for municipal revenue bond offerings and thereby reduce interest costs. The investment bankers deny the contention. No action has yet been taken by the Congress on these bills.

Maturity schedules and call features -- Borrowers can choose among a number of alternatives, both as to maturity schedules and call features. Ordinarily, bonds should not be issued for a length of time that exceeds the expected life of the project. In fact, many State laws set forth the maximum duration of bond issues for different kinds of projects.

1/ Alfred T. Harris, "Deep Discount Tax Exempt Bonds -- Who Buys Them -- Why?", The Bond Buyer, Special Convention Issue, No. 1, November 30, 1964.

2/ U. S. Congress, House, Committee on Banking and Currency, Hearings, Increased Flexibility for Financial Institutions, 88th Congress, 1st Session, 1963.

It should be borne in mind that the longer a maturity schedule, the higher the interest cost, both because of the additional interest paid for each additional year of maturity and because a longer average maturity can be expected to require a slightly higher rate. Therefore, in the interest of economy, a maturity schedule should be as short as possible. Other factors also enter into the determination of a maturity schedule. For example, possible obsolescence may dictate retirement of the debt much sooner than the expected life of the project. An examination of the maturity schedules of already outstanding debt may indicate the need to arrange maturities for the proposed debt issue in such a way as not to burden unduly the budgets of years with particularly heavy debt maturities. The desires of the investors at the time bonds are offered will also affect the kind of maturity schedule indicated.

Whether or not to include a call feature in a particular debt offering is another matter to be decided by those planning a local government bond issue. A "call" provision in a bond indenture allows the borrower to retire all or part of a bond issue before it matures. Such a feature is advantageous to the borrower in a market with a downward trend in interest rates. However, the borrower pays a premium for the privilege of including a call provision, because it makes the bond less attractive to the investor than one not callable.

THE INEFFECTIVENESS OF EXISTING STATE POLICIES CONTROLLING LOCAL DEBT MANAGEMENT

The legalistic debt controls to be found in most States and the administrative debt controls in a few States stem directly from State action to correct local borrowing situations that have resulted in widespread default. Thus, in the 1850's and 1860's, following a rash of municipal borrowing to help finance railroad construction, and subsequent defaults, State constitutional and statutory enactments prohibited municipalities to lend their credit to, or subscribe to the stock of, a private business. Most of the provisions limiting local indebtedness to a fixed percentage of assessed valuation and requiring voter approval of proposed bond issues were depression-born, largely during the 1870's, and the few instances of State administrative regulation of local debt originated mainly during the Great Depression of the 1930's. 1/

1/ Leonard E. Goodall, State Regulation of Local Indebtedness in the United States, Arizona State University, Bureau of Government Research (Tempe: 1964), Research Study No. 9.

The Traditional Legalistic Approach

The traditional legalistic approach is characterized by two common constitutional and statutory restrictions on the debt powers of local government; (a) a limit on indebtedness expressed as a percentage of the local governmental tax base, and (b) requirement of a local referendum to authorize the issuance of bonds, often calling for some kind of special majority, e.g., 60 percent, 65 percent, or two-thirds favorable vote. 1/

The general indictment of this approach to local debt control is set forth in the Advisory Commission's report State Constitutional and Statutory Restrictions on Local Government Debt and it can be summarized in the following nine-point bill of particulars:

1. It pertains to present or past conditions, rather than those of the future when long-term debt will be subject to servicing, and thus takes no account of divergent trends for various governments and communities.
2. It deals with separate layers of local governments rather than the aggregate of local government for a particular area.
3. It purports to measure economic capacity by reference to only one revenue source, the property tax, which provides less than half of the revenue of most local governments in most States.
4. This type of limit is, in most States, imprecise and potentially discriminatory because of the nature of the property tax base to which it refers. The real level of limitation is determined by local assessment practices rather than being closely governed by the legal provisions.

1/ For a State by State analysis of restrictions on local government debt, see, Frances L. Starner, General Obligation Bond Financing by Local Governments: A Survey of State Controls, University of California, Bureau of Public Administration (Berkeley: 1961).

5. Being commonly applicable only to full faith and credit debt, this type of limitation offers no assurance that aggregate local debt will be kept within prudent bounds.

6. Debt restrictions have probably restrained the total volume of local government borrowing to some extent, but the extent to which this is true cannot be definitely measured.

7. The restrictions have been an important factor in the rapid recent growth of nonguaranteed local debt, as against full faith and credit borrowing. This development has a differential effect among various purposes of local borrowing and various types of local governments. It tends to increase the cost of borrowing, through higher interest rates and more extended bond maturities. It also is likely to impose more rigidity on local governments' future budgeting than would full faith and credit borrowing.

8. Debt restrictions have tended to impair the public accountability and responsiveness of local governments in various ways, including the promotion of special districts and various kinds of financing authorities, and the complication and obfuscation of financial arrangements.

9. The restrictions have affected governmental relations in various ways. They may artificially increase the need and demand for Federal and State grants to local governments. In some States they have contributed to urban-rural and local-State frictions.

The Coercive Administrative Approach

In theory, States could take the coercive administrative approach as a means for controlling both the quality and the quantity of local debt issues, but in practice this solution would be virtually impossible to effect. For most States the exercise of strong administrative control over local debt policy would represent a radical departure from the existing pattern of State-local relations which is characterized by a high degree of local autonomy. Thus, in the absence of a severe crisis situation --

widespread default on local bond issues -- any such proposal would receive scant public support.

Even in the three States where State administrative control is exercised over the bond issues of all local governments, coercion is more apparent than real. Louisiana's Bond and Tax Board, Michigan's Municipal Finance Commission, and North Carolina's Local Government Commission exercise complete control over local borrowings. The Louisiana Board, though having the widest powers of any of the three, has too small an appropriation and too small a staff to afford a fair trial. The Michigan and North Carolina Commissions pass upon local economic ability to pay debt and the legal form in which the obligations are offered for sale. To the North Carolina Commission is given the authority, which the Michigan Commission lacks, to decide whether the bonds and notes are "necessary or expedient." 1/ Despite this substantial grant of legal authority, the Michigan and North Carolina Commissions do not disapprove very many debt applications.

There are at least three reasons for the high approval rate of local bond issues. First, State and local officials in North Carolina and Michigan consult in the early and fluid stages of planning and obligations so that many proposals may be modified without coercion. The absence of definitive fiscal criteria is another reason why relatively few local applications to borrow are disapproved on the grounds that they are unnecessary or inexpedient. Third, and most important, bonds in both Michigan and North Carolina are normally subject to voter referenda which express community opinion as to necessity. In short, the Michigan and North Carolina experience points primarily to the value of persuasion and technical advice and only incidentally to State coercion.

1/ However, the North Carolina law does not define either of those terms.

Chapter 2

A BASIC PLAN FOR STATE TECHNICAL ASSISTANCE

The basic technical assistance program described in this chapter is designed to maximize the amount of information that can be made available to investors for evaluating local government debt offerings and to local government officials for marketing such offerings, at the same time holding to an irreducible minimum the amount of State involvement in local fiscal management. To accomplish those purposes, a basic assistance plan should contain at least the following key elements:

1. Simplification and modernization of the debt laws;
2. Development and maintenance of a State file on local debt and related data;
3. Dissemination of data on local government finances;
4. Prescription of minimum standards for official statements on local debt offerings; and
5. Development of an educational program for local finance officers.

Placement of these responsibilities within the State organizational framework will vary, depending upon circumstances in particular States. Those States that now have, or may in the future create, an agency exercising a broad advisory role with respect to local government affairs, will undoubtedly lodge the debt technical assistance function in such an agency. Others will place this responsibility with the agency that administers State debt. Still others may give the responsibility to some other State fiscal officer -- the comptroller, or the auditor, or the tax or revenue commissioner. In any event, the debt assistance function should be placed wherever the technical competence is available or can be developed.

CODIFICATION AND MODERNIZATION OF DEBT LAWS

The State constitution and statutes, together with court decisions and attorney generals' opinions, constitute the legal framework within which local debt is issued. To the extent this body of law can be put in some logical order, the task of legally validating proposed bond issues can be simplified and the costs connected with this process can be reduced.

This Commission recognized the problem in an earlier report, when it stated: 1/

As a minimum, and an essential starting point for various other efforts, most States could benefit by an intensive effort to assemble and codify existing statutory provisions that pertain to the indebtedness and borrowing power of local governments. Such action alone would expose more fully the widespread existence of overlapping and contradictory provisions which have tended to hamper sound financial administration by local governments and to limit the ability of State legislatures to deal intelligently with this subject.

As the foregoing quotation notes, the codification process will itself point up areas that need improvement. Most State debt laws contain outmoded and unduly restrictive sections, and this Commission has made a number of recommendations to modify some of the constitutional and statutory restrictions on local government indebtedness (see Appendix A). While the present report makes no additional policy recommendations, a number of questions may be raised as to potential improvements in various aspects of debt management. For example, in re-examining its debt laws, a State may wish to consider whether or not to prescribe the use of serial bonds for all debt issues, and, if serial bonds are prescribed, whether localities should be allowed discretion in arranging serial maturities during the term of the bond (a) so that the particular issue dovetails into the debt service of all bonds, and (b) to prevent the undue shifting of the larger maturities to later years.

1/ Advisory Commission on Intergovernmental Relations, State Constitutional and Statutory Restrictions on Local Government Debt, (A-10) September 1961.

Another question that might be raised is whether to require strict adherence to the principle that the term of a bond issue should not exceed the expected life of the improvement, or whether other criteria should be sought. The answers to these and other questions, which would vary from State to State, would lay a firm foundation upon which to build a system of State technical assistance to local debt management.

STATE FILE OF LOCAL DEBT AND RELATED DATA

The full disclosure of detailed current information on the financial, economic, and social characteristics of a debt-issuing local government is essential to its realizing the best possible borrowing terms. Failure to make such data available to the rating services and investors has been identified by Moody's as one of the pitfalls in issuing public bonds. 1/

To make sure that the detailed information needed by investors, public officials, and security analysts is available to them, the State should maintain a file of debt and related data for each of its local governments. Such a file would contain not only the details relating to each local outstanding bond issue, but also information on prospective bond issues, the results of bond elections, assessed and equalized values, tax rates and levies, tax collection experience, general financial data, and demographic and economic data. In effect, this file would constitute a series of "community profiles."

Sources of Data

The information for the State debt file would be derived from a variety of sources. Much of the information would come from the debt and general financial reports, budgets, audits, and capital improvement programs published by the local governments themselves. To insure comparability of the data among local governments, the State agency should prescribe a standard classification framework for all local governments, with variations tailored to the needs of particular kinds of government. A number of States -- including

1/ Moody's Investors Service, Inc., Pitfalls in Issuing Public Bonds, (New York: April 1963), p. 20 ff.

California, New Jersey, and New York -- require all local governments to file detailed general financial reports on standard forms provided by the State. Some States restrict their reporting requirements to counties or school districts. Others, like Massachusetts, prescribe the content of local audit reports, which are prepared by State personnel.

Debt and general financial reports -- The audit report, the general financial report, and separate debt reports are the vehicles through which State agencies keep informed on local debt incurrence and retirement and related processes. Three purposes are served by those informational sources. First, aggregates of debt are reported for each local government by the term, purpose, and character of liability of debt incurred, retired, and outstanding. Such aggregates are necessary for an appraisal of inter-year debt trends and of inter-unit comparisons during the year. Second, related information is indispensable to an evaluation of past and prospective debt loads by showing assessed valuation, revenue classified by tax and other sources, payments for debt service classified by debt liability, and other expenditure classified by function and by character and object.

Third, to be useful to security analysts and public officials, debt data must be presented in some detail. Accordingly, outstanding debt must be shown by individual bond issue as to date of issue, amount, purpose, term, interest rate, and annual requirements for interest and debt retirement. Each capital improvement or bond fund requires separate reporting. Each sinking fund or debt retirement fund needs reporting as to assets and liabilities, investments, and annual transactions. The extent to which localities have encumbered their legal borrowing capacity, verifying the validity of deductions from gross debt, is of concern alike to officials, taxpayers, and bond investors.

State agencies assemble the three types of information by different methods, depending upon the nature of their responsibilities. 1/ In Massachusetts, the Division of Municipal Accounts extends advisory assistance to municipalities and exercises control only in passing upon town notes and emergency loans. Reporting to the State consists of the annual municipal audit, containing

1/ Information as to types of local reports filed with the States, of which Massachusetts, Michigan, and New Jersey are illustrative, is derived from report forms assembled from State agencies.

selected classifications of debt detail; the annual report of receipts, disbursements, and debt for which aggregates suffice by reason of audit information; and an annual single-page summary of debt within and outside the debt limits.

New Jersey has broader debt supervision through advisory assistance, the check of debt against limits, the certification of debt service due the next year, and the authorization of borrowing in excess of debt limits. New Jersey's required reporting, therefore, is wider in scope than Massachusetts' reporting. Including audits and budgets, the reports required by New Jersey comprise:

1. The annual audit -- contains selected debt breakdowns;
2. The annual financial statement -- reports trial balances of operating and capital funds, debt service transactions, capital outlays authorized and expended, a list of bonds issued during the year, and detailed receipts and disbursements;
3. The annual debt statement -- shows a detailed record of gross debt and deductions to arrive at net limited debt, assessed valuations, itemization of bonds and notes outstanding and authorized;
4. The supplementary debt statement, filed before bonds are issued -- updates the annual debt statement by showing information to compute used and unused parts of legal borrowing capacity; and
5. The annual budget -- contains classified fund transactions to reveal whether State budget and debt codes are observed, capital outlays and debt service appropriated and expended.

The Michigan Municipal Finance Commission, a debt regulatory body, passes upon all local bonds and notes before their issuance, checks the sufficiency of pending tax levies to pay debt service the following year, and approves transfers from and to sinking and debt retirement funds. In the absence of audit and budget reports, the Michigan Commission assembles the following reports (aside from applications to borrow):

1. Comparative statement of assets and liabilities -- shows the previous and current years;

2. Summary of cash receipts, disbursements, and balances -- summarizes each debt, capital, and operating fund;

3. Detailed debt, assessed valuation, and tax levy report -- shows assessed and equalized valuations, tax rates and levies, and itemizes outstanding obligations by amount, character of liability, amounts and due dates of debt maturities, interest rates, and fund balances available for bond payments;

4. Sinking fund reports -- summarize receipts and disbursements, itemize investments, and report assets of each callable refunding bond;

5. Receipts and disbursements of debt retirement funds -- summarizes transactions, including transfers to and from funds;

6. Annual general report -- classifies receipts and disbursements and shows transactions of special assessment fund.

Annual budgets -- In addition to requiring that local governments report on the results of the previous year's financial debt operations, a number of States call for the filing of local budgets. This requirement makes a valuable informational source available for State technical assistance to local borrowing operations. By showing figures for three years -- the past, current, and next year -- the budget updates information as to relative revenues and comparative expenditures for debt service, capital purposes, and current operations. Changes from previous years in the income and outgo sides of the budget make visible information lacking in audits and reports of past transactions. A number of State-prepared forms contain detailed data or appended exhibits of debt, debt service, and capital expenditure that are useful for technical assistance to borrowing operations.

Another budget plan, useful for such assistance, is to require the local filing of budgets, before final adoption, with a State agency for review to assure that bona-fide budgets have been drafted.

Essentially, the review determines whether or not statutory fiscal regulations have been complied with in a satisfactorily prepared budget form. Local purposes and amounts are untouched except for charges for debt service, reserves, and any other mandatory obligations. State review before final local adoption of the budget, assuring adequacy of debt service and safeguarding against deficits and funding bonds, has proven successful for all local governments in New Mexico and New Jersey and for counties in California, Florida, and Kentucky. Either with or without State review of this type, the local filing of budgets with a State agency will provide a useful tool for State technical assistance to local borrowing operations.

Capital budgets and long-term programs -- No aspect of budgeting is of more importance to debt technical assistance than the planning of a long-term capital program. Indispensable as are data of the past and current condition of local governments, debts are paid in the future; and a knowledge of future financing, even on an estimated basis, is a tool of the first importance in both the local and State evaluation of proposed bond issues.

This study is concerned with four elements of planning: 1/

1. The capital improvement program is stated in terms of the physical improvements required for a specified period of years in the future. Such a program is the creation of a community, normally through a local planning agency, that should start with a physical inventory of capital improvements and be extended into the future by an appraisal of replacements of existing assets and the addition of future improvements.

2. The capital budget should correlate capital improvement receipts, comprising long-term bonds, short-term notes, and various revenue sources, with capital expenditures arranged by priorities for a specified number of years.

1/ For discussion of local planning and capital budgeting, see International City Managers' Association, Municipal Finance Administration (1955) pp. 339-340; Municipal Finance Officers Association of the United States and Canada, Budgeting with Special Reference to Capital Budgeting (1956); and Lemox L. Moak and Kathryn W. Killian, A Manual of Suggested Practice for the Preparation and Adoption of Capital Programs and Capital Budgets, Municipal Finance Officers Association of the United States and Canada (1964).

3. The long-term program should incorporate the capital budget and should include debt service on outstanding and proposed obligations as well as the current operation cost that is importantly affected by the nature of future capital improvements.

4. The annual budget, to which the community is legally committed, would set forth one year of the long-term program, the later years of which are subject to annual revision.

The four-fold elements have been most effectively expressed by local initiative, often through local planning boards or agencies and at times with the guidance of professional planners. Background studies, such as the demographic and economic composition and prospects of communities, are gradually spreading among American cities and to a lesser degree among counties. The State agency extending debt technical assistance should assemble and use local planning reports, such as capital budgets, long-term programs, and economic background studies.

The usefulness, indeed the necessity, of long-term capital planning cannot be overemphasized. While most States have statutory requirements as to annual budgeting by local governments and some require the filing of local operating budgets with State agencies, the need for a capital budget is only beginning to be recognized. The States should foster the development of local capital budgets and, in conjunction with their programs of technical assistance to local debt management, should require that such budgets be filed with the State agency administering such assistance.

Additional information -- Many State tax or revenue agencies gather information on local assessed valuations, property tax rates, and tax levies. States with property tax equalization programs also have information on equalized and full property values. In addition, some State economic development agencies maintain files on the economic characteristics of local governments -- for example, types of industry, employment and unemployment, retail sales. In addition, the State debt advisory agency should be acquainted with the kinds of data provided by the U. S. Bureau of the Census on population, housing, government finances, etc., and should add all relevant facts to the local debt file from those sources.

PUBLICATION OF DATA

While the development and maintenance of a debt file will serve the detailed data needs of underwriters and rating services, States should also disseminate information on the finances of their local governments for more general use. Such a publication should abstract such salient facts from the debt file for each local government as: population; total debt outstanding, issued, and retired, by type of debt; a historical record of property tax collections and delinquencies; assessed valuation and full value of real and personal property; tax rates; and revenue by source and expenditure by function and character (operation, capital outlay, debt service, and subsidy payments). In addition to providing such information for each local government (possibly with some telescoping for the very small governments), the report should present statewide aggregates for all local governments and for types of governments (for example, cities, counties, and school districts). It should also contain some historical data as well as per capita figures to permit inter-unit comparisons. Such a publication should be released as soon after the reporting period as possible.

Too often, States gather audit and financial reports and merely file them away. Few States prescribe standard reporting classifications -- among the notable exceptions are California, New Jersey, and New York -- and only a limited number disseminate the information they gather in any meaningful way on a current basis. More than half of the States publish some kind of information on the finances of their counties and municipalities, including debt statistics. In addition, most State education agencies publish local school district data.^{1/} However, most of the reports are sketchy, and few appear sooner than two or three years after the end of the period for which they are reporting.

A comprehensive annual State publication on local government finances of the kind described above is useful for general public consumption and for research purposes, even if it is issued a year or two after the end of the period to which it relates. However, information, in somewhat less detail, on the finances of individual

^{1/} U. S. Bureau of the Census, State Reports on State and Local Government Finances, 1962 Census of Governments, Vol. VI, No. 3, pp. 36-48.

local governments should be made available to potential investors and State and local government officials on a more current basis -- probably within six months of fiscal year endings. To this end, the States should consider issuing a series of reports, one for each type of local government, based on preliminary data required to be submitted by the local governments on standardized schedules. These reports would emphasize the data for individual local governments and not statewide aggregates, so that, in the interest of current reporting, publication need not be delayed until the schedules of all local governments are obtained. A preliminary report of this kind would be useful even if it were to encompass the data for only 75 or 80 percent of the governmental units. Information on the missing units would be incorporated in the later, more comprehensive annual report.

STANDARDS FOR OFFICIAL STATEMENTS ON LOCAL DEBT OFFERINGS

When local governments set out to borrow, they are selling a commodity on the market -- in this case, the investment market. In the usual situation, the bonds are sold in the first instance to an underwriter -- the wholesale dealer in securities -- who then markets them at retail to individual investors or to insurance companies and other institutional investors.

As in the successful marketing of any commodity, "it pays to advertise." Moody's has singled out as one of the pitfalls in issuing public bonds "the failure to advertise the issue the right way in the right places." 1/

Two types of statements and publicity are normally used to acquaint the public in general and bond dealers and investors in particular with prospective sales of local bonds and notes. The first, the notice of sale, deals essentially with the mechanics of sale by specifying the amount, term, place and date of sale, and similar data. The second, the sales brochure or bond prospectus, is the presentation of financial and economic information by which possible buyers may appraise the offering and be induced to bid on the securities.

1/ Moody's Investors Service, Inc., op. cit., p. 38.

The States would be well advised to provide statutory standards to their local governments as to the content of the advertising notice and the bond prospectus. This Commission has gone on record in recommending this form of local debt regulation to the States. In its discussion of this recommendation the Advisory Commission commented as follows: 1/

The one form of direct State regulation we do suggest here concerns the content of official statements prepared by local governments in connection with their issuance of long-term debt. Professional and underwriting organizations have developed valuable recommended standards, and the credit standing of numerous individual governments has been aided by their voluntary application of such recommendations. However, many local units are still penalized in their issuance of debt by inadequate official statements, which fail to provide the background needed by underwriters and investors in evaluating the securities involved. State action to set minimum standards for such statements should benefit the prospective borrowing units themselves and tend broadly to improve the market for local government bonds.

Sales Notice

The sales notice is the vehicle by which local governments notify the investors that they are about to enter the bond market. The investors' services and the Investment Bankers Association have spelled out the types of information that should appear in sales notices. The latter organization provides a list of 20 items: 2/

- (1) legal name of the issuing body;
- (2) amount and purpose of the bonds to be sold;
- (3) date, hour, and place that bids will be opened;

1/ Advisory Commission on Intergovernmental Relations, op. cit., p. 83.

2/ Investment Bankers Association of America, Fundamentals of Municipal Bonds, (Washington, D. C.: 1963), pp. 35-36.

- (4) date of bonds, maturity dates, and option dates if bonds are callable;
- (5) when and where interest and principal are payable;
- (6) bond denominations, and registration privileges;
- (7) basis for bidding;
- (8) basis for award;
- (9) notice that the right to reject bids is reserved and whether bonds below par or conditional bids will be accepted;
- (10) amount of certified check or bank draft that must accompany the bid and to whom it is payable;
- (11) name of bond attorney whose approving legal opinion will be furnished;
- (12) name and address of official to whom bids should be submitted;
- (13) time and place where the bonds will be delivered;
- (14) whether the local government or the purchaser will pay for the legal opinion and the printing and delivery of the bonds;
- (15) what provision has been made for payment of principal and interest (debt service payable from unlimited or limited property taxes, or special taxes or assessments, or revenue from a utility or enterprise, or from a combination of sources);
- (16) tax rates of issuing government and of overlying governments, and statement of any constitutional or statutory debt or tax restrictions;

- (17) statement of previous default record, if any;
- (18) population according to latest Federal census, and an estimate of present population;
- (19) statement that purchaser will be furnished with closing papers, showing that no litigation is pending or threatened; and
- (20) name of person who will furnish additional information about the local government and the bond sale.

State statutory prescription need not be in such detail, but rather should serve as a guide to the State agency that is authorized to outline the content of sales notices. In New Jersey, for example, the notice of sale, under statutory direction, must contain the following basic data to which is coupled recommended discretionary information: (1) the principal amount, designation, date of issue, denomination, and maturities of the bonds offered for sale, (2) the rate or rates of interest, (3) the terms and conditions of the public sale, and (4) such other information as may be determined by the governing body. 1/ The New Jersey notice of sale must be advertised both in a local newspaper and in a financial journal.

In New York, the State Comptroller's Office regulates the form, publication, and mailing of notices of sale. 2/ Different notices are mandatory, not only for bonds and notes but also for different types of local government. Among the classes of information required are a description of the bonds or notes according to amount, purpose, date, denominations, maturities, time of debt service payments, whether the bonds will be registered or callable, the medium and place of payment of principal and interest, and the time and place of delivery of the securities. The potential bond buyers must be assured that the pending issue is within the debt limit by comparing the total allowable debt with the net limited debt, or by indicating that the State Comptroller or the Board of Regents has approved school bond issues in excess of the legal limit. Notices of sale are mailed to financial publications and to investors' services, and local officials are urged to circularize the notices among many New York bond dealers.

1/ New Jersey Revised Statutes, Title 40-A: 2-30 and 31.

2/ New York Local Finance Law, Secs. 57.00 and 60.00.

Michigan statutes require the advertising of notices of sale of bonds and notes, except for small issues, and vest in the Municipal Finance Commission the authority to prescribe minimum information for the notices. 1/ The procedural steps in the sale, describing the issue and the terms of sale, methods of computing interest and offering bids, are outlined in forms furnished to local officials. Security for debt service is emphasized by the Michigan agency in differentiating between information called for by general obligation bonds, special assessment bonds, revenue bonds, and mortgage bonds. Publication of the notices, both in a local newspaper and in a financial journal, is mandatory.

Official Statement for Appraising Bond Offerings (Prospectus)

In addition to the sales notice, an official descriptive statement or debt prospectus is needed so that potential bond buyers can appraise the financial records and economic and other characteristics of the borrowing community. Dr. Frederick L. Bird, when Research Director in the municipal department of Dun & Bradstreet, pointed out this need for New York City: 2/

It is necessary to understand, and have consideration for, the investor's point of view; to determine what he wants to know, and properly should know, about the city financial affairs; to provide such data in readily understandable form.... Each sale should be preceded by publicity designed to give potential bidders and investors adequate notice and also pertinent, up-to-date financial information so well presented as to attract special attention. Thus the prospectus should go to a comprehensive mailing list well in advance of the date set for receiving bids, in a few pages should present as clearly, simply, and effectively as possible not only basic financial statistics but data on the various important security factors that govern the issuance and administration of the city's debt. The opportunities for strengthening the city's financial standing that stem from such a statement, if skillfully prepared, are great.

1/ Michigan Public Acts of 1943, Act No. 202, Sec. 2.

2/ The Municipal Debt: A Description, Analysis and Appraisal of Debt Policy and Administration of the City of New York, (Mayor's Committee on Management Survey of New York, New York: 1951), pp. 128-129.

Since Dr. Bird's observations were in order for New York City, the largest non-federal governmental borrower in the United States, similar observations would be warranted for many other local governments across the nation. To an encouraging degree, municipalities have voluntarily undertaken to issue official statements of the type described. The informational gaps, however, are many. To prescribe the format of a debt prospectus is difficult because of the diversity in the nature of local governments.

With respect to prospectus standards, the State should have a twofold objective: (a) to prescribe minimum standards; and (b) to encourage as many localities as possible, through improved accounting and reporting practices, to go beyond the minimum level.

New York invites attention because it neither sells local obligations nor reviews pending issues, except for special classes. Prescription of minimum standards for all local governments, termed a "Report of Essential Facts," is one aspect of the regulatory power exercised by the New York State Comptroller over notices of bond sales. The following outline recapitulates the chief features of the New York report:

1. Description of community -- Population for four years (census or estimated); school census; area; citation of any special charter; type of community in which bond-issuer is located; and public and private facilities in the area.

2. Trends for preceding five years -- Debt as to total amount, deductible items, and net debt; expenditure by major character classes; assessed valuation of real estate (personal property exempt); state equalization ratio of assessed to full value; real estate tax rate and levy; other revenue, by major class.

3. Selected tax detail -- Three-year record of property tax collections and delinquencies; description of tax collection machinery, especially regarding delinquencies, penalties, and tax sales; itemization of local nonproperty tax revenue for three years.

4. Assets of funds -- As of specified dates, assets of sinking, capital reserve, repair reserve, tax stabilization, debt reserve, and other funds.

5. Bond principal maturities -- Amounts maturing in each of next 10 years, excluding and including the bond issue to be sold.

6. Revenue producing enterprises -- Confined to showing (a) principal maturities for such enterprises included in No. 5 above, and (b) debt for such enterprises excluded by State Comptroller's approval from debt subject to limitation.

7. Finances of overlying or related units -- For large cities fiscally responsible for schools, a separate itemization of school debt, expenditure, debt service, and taxes; itemization of net debt of special districts situated in a city, village, or town; special improvement district debt included in town debt; optional reporting of debt and tax records of all other overlying school and special districts.

8. Other information -- Statutory authority for the purpose for which bonds are to be issued; statement whether any debt principal or interest is past due; statement whether procedure for validation of bonds has been or is to be complied with.

Instead of outlining the content of minimum standards, this study employs a twofold approach. First, it suggests that each State adapt the Investment Bankers Association's reporting format to its particular needs ^{1/} (see Appendix B). Second, the outline below offers for consideration a set of reporting principles and methods, developed from the best current practice, which should underpin the construction of a sound prospectus.

Variations in informational requirements -- A State comprises communities that differ widely in size, resources, functional responsibility, and governmental organization, and in the kinds of

^{1/} Fundamentals of Municipal Bonds, *ibid*, pp. 44-50. Consult also publications of the Municipal Finance Officers Association of the United States and Canada: Marketing Municipal Bonds (1946), Preparing the Bond Prospectus (1955), and Evaluation of Municipal Securities as a Guide to Better Financial Reporting (1958).

obligations they can incur. The kinds of information included in the bond prospectus will vary accordingly.

1. Character of liability -- Axiomatically, different forms are required for general obligation bonds and for revenue bonds. With regard to debt service protection for general obligation bonds, full disclosure of the local government's general finances is essential. Investors in revenue bonds require a detailed statement on the financial condition of the proposed facility, including an explanation of liens, covenants, reserves, and other protection to bond buyers. These two major types, however, do not satisfy the needs in all States. Separate forms may be required, depending on the State, for nonproperty tax bonds (payable from gross receipts and other nonproperty taxes), bonds payable from property taxes subject to limits, special assessment bonds, housing authority bonds, and bonds secured by pledges of two or more revenue sources.

Some States do not authorize local revenue bonds, or, if authorized, some municipalities may prefer to pledge full faith and credit to bonds issued to finance revenue-producing enterprises. The bond buyer, consequently, must look both at general and enterprise operations. Even if revenue bonds are issued extensively in a given State, a bridge between the two types is desirable by including (a) in the general obligation form a trend report of enterprise debt, income, expense, debt service, and surplus or deficit, and (b) in the revenue bond form a summary of general debt and related information that reacts upon the entire credit standing of the community.

2. Population size -- Although factors for judging credit may be similar for large and small communities, the extent and even the exact nature of the financial and economic information may vary between them. Municipalities and counties under 50,000 population would be amply reported by a simpler form than the detail expected of larger communities.

3. Type of government and function -- Schools afford the most obvious example for a separate form. They differ always as to function, and also as to type of government in most States. In a number of States, nearly all on the Atlantic Seaboard, part or all of the school districts are dependent units of local general government, and both school and general financial data are necessary to appraise credit quality. Municipalities, counties, and special districts often differ so widely as to functional responsibility, resources and revenue, and debt incurrence that standard forms for general obligations may well be tailored to fit the patterns of

governmental types in individual States. Similarly, forms for revenue bonds may be tailored to fit the different operative records of different major enterprises, whether an electric power, water system, or self-sustaining sewerage system.

Basic informational requirements -- The following kinds of information should be included in all bond prospectuses:

1. Legal authority and debt incurring power -- Common to all standard forms should be the citation of the legal authority to borrow and spend money for the purpose for which the bonds are to be sold. For general obligations, a summary of debt incurring power could be confined to a comparison of the amount permissible under the debt limit with the gross debt, allowable deductions, and net limited debt. The bond attorney's favorable opinion of the legality of the issue, even if preliminary, should be either cited or summarized.

2. Summary of past financial trends -- To depict the trend the financial condition of the local unit is taking, the forms should summarize basic data for selected prior years by showing total debt as to character of liability, revenue and expenditure as to major category, total assessed and full valuation, property tax rates and levies, property tax collections and delinquencies, and the record as to any defaults or refundings to avert defaults. Trend data obviously differ among types of debt liability. Meaningful trends are disclosed by comparisons of the tenth and fifth previous years with the last two years.

3. Detail for latest completed year -- The borrowing unit can readily report detail, provided it is confined to the latest year, and the credit analyst is helped by an itemization of outstanding issues, showing amount, purpose, interest rate, and principal and interest due. For a metropolitan center, however, the debt detail should be reserved for an accompanying annual report. For all borrowing units, the revenue side for the previous year requires itemization of each main source to reveal in particular the relative size of each nonproperty tax, and revenue from State and Federal governments classified as to use for operation, capital outlay, and debt service. On the expenditure side, the credit analyst needs to learn not merely aggregates by character (i.e., operation, capital outlay, etc.) but the extent to which responsibility has been assumed for individual functions in the previous year.

4. Future trends -- Since the bonds to be sold will be paid in the future, many credit reports now set forth the future debt

service on outstanding debt and on the bonds to be sold. While an itemization for all years during which bonds will mature has advantages, a listing for the next 10 years would be acceptable because of the likelihood that later issues will change the maturity schedule. In any States adopting plans for the review of prospective bond issues as outlined in Chapter 3, the inclusion of a future capital budget would be feasible in all credit reports. In the absence of the adoption of the suggested plans, the credit report should (a) specify all bonds authorized but not issued, and (b) summarize all capital improvements and bond issues that are likely during the next six years. Indispensable to the sale of revenue bonds is an engineering estimate for the next six years of revenue from the facility or service, operating cost, other charges against revenue, and the anticipated surplus margin.

5. Overlying, coterminous, and underlying local units -- Usually credit reports depict the net general debt, tax rate, and tax levy not only for the borrowing unit but for all units levying taxes on the property within the boundaries of the borrower. For municipalities and school districts, except county systems, the additional data are for shares of overlying units; for counties and county school districts, the added data are the totals for underlying units; and in some cases, usually municipalities and districts, added data may be for coterminous units.

In a simple governmental structure, the local officials alone can obtain the aggregate statistics. In complex structures, and especially for county brochures showing underlying units, the State agency should -- as for any other aspect of the credit report -- cooperate with the local officials by making data available from State files. With the increasing importance of local nonproperty tax revenue and intergovernmental revenue, a realistic report would set forth similar summaries of classified revenue and expenditure.

6. Physical volume of services -- With standard forms tailored to fit types of government, liability, and selected functions, credit reports would acquire an added dimension by showing the physical volume of services. For example, the debt prospectus outline for the Michigan Department of Public Instruction calls for the concise analysis of present and future school building needs of a school district. 1/ Elementary and junior and senior high schools

1/ Department of Public Instruction, Local Programs for Financing School Building Programs (Lansing: 1958), p. 20.

are separately reported as to capacity of (a) existing adequate school houses, (b) existing unsatisfactory school houses, (c) school houses under construction, and (d) school houses to be financed by proposed bond issues. Additional school houses required during the next two periods of five years are recapitulated as to number of buildings and classrooms, capacity, and estimated cost.

Utility services are reported as to physical volume in some, though far from all, credit brochures. Interyear comparisons are feasible for electric power systems as to KWH's generated, purchased, or sold, and the classified number of customers at the end of each year. Water systems may also be reported as to supply, consumption, and classified number of consumers. Highway and street mileage, classified by type of existing construction and compared with programs for future surfacing, may be summarized in many counties and cities.

7. Economic characteristics of the community -- Local governments are handicapped in working up the necessary economic base data for evaluating debt and fiscal loads. While the typical prospectus shows assessed valuation (and should set forth estimated full valuation), the swing to nonproperty taxes now requires the reporting of other economic characteristics both for general obligations and revenue bonds. Conventional reporting involves the identification of chief industries, if possible by dollar value of production, and at times by the listing of the names and property value of the leading companies. Transportation facilities are often listed.

Among the assortment of data that have been urged for reporting and sometimes used to good advantage are retail and wholesale sales, service establishment receipts, consumption and number of consumers of publicly and privately owned utilities, and the number and value of building permits. Local nonproperty taxes and State taxes derived from the local community are often overlooked. Economic indicators are more often available on a countywide basis than for smaller areas.

To the customary reporting of total population for several Census years and an estimate for the latest year may well be added a classification by age group, school enrollment, and in some areas of the employment and unemployment rates. Mention of the area and density of population indicates the compactness of the jurisdiction and the probable extent of development of the area. Interyear comparisons, at times on a per capita basis, are helpful in evaluating the stability, volatility, and diversity of the economy, and prospect of economic growth of the community.

8. Quality of public administration -- A debt prospectus can provide some clues as to the general character of the local government and the quality of its administration. Among these are: an indication of the nature of the local government organization and financial administration, especially as to accounting and debt management responsibility, the existence or absence of planning and zoning ordinances and agencies, the accounting basis (cash, accrual, or combination thereof), and tax and revenue collection methods and the handling of tax delinquency.

9. Inclusion of notice of sale advertisement in debt prospectus -- The advertisement of the notice of sale, considered in the previous section, should be incorporated in the prospectus, together with a bid offer form, for circularization among bond dealers.

Suggested Legislation

The suggested legislation (see Appendix C), in requiring minimum standards, describes them only in general terms while authorizing the State agency to spell out the details. Local officials could, of course, exercise their discretion in reporting information in addition to the minimum content. Forms could be prepared jointly by local and State officials.

EDUCATIONAL ACTIVITIES

Just as many State tax agencies are now providing in-service training for local assessors, so should the States be instructing local finance officers in the intricacies of borrowing money. Small communities, which enter the money market infrequently, do not have to employ the technical competence that is needed in connection with a bond issue. However, even the smallest community employs someone with responsibility for its finances, and this individual should have access to guidance and training in some of the technical aspects of the bond market. Out of such a training program would develop reference materials spelling out the steps to be taken in issuing bonds and the pitfalls to be avoided. The State would thus make available the technical competence of its own fiscal experts as well as that of the universities and the professional organizations.

Debt Manuals

States should assist local governments with their debt management problems by issuing bulletins and manuals to serve as guides in debt

incurrence and retirement. The monthly or other periodic bulletin or newsletter could be used by State agencies to explain new laws or amendments and opinions of the courts and attorneys-general, or to outline revised debt and related procedures. Special releases or pamphlets have been issued, and can be employed more extensively, to familiarize local officials with special subjects -- revision of debt limits, capital budgeting, provisions for revenue bonds, and other topics. The manual has been a widely used device for outlining local accounts or audit standards, but awaits full development for local debt. Examples for general local government are A Guide to Pennsylvania's Municipal Borrowing Act of the Pennsylvania Bureau of Municipal Affairs, the borrowing chapter of the Ohio Handbook for Village Officers of the Ohio State Auditor, and A Guide for Preparation of Bond or Temporary Note Transcripts of the Kansas Attorney General. That manuals fill a definite need is shown by their wide circularization by State educational agencies in Michigan, New York, and several other States. Across the nation, nevertheless, debt manuals are the exception rather than the rule.

Training

Although some local officials obtain valuable information from the programs (conferences and publications) of various State and national professional associations, the States can make a significant contribution on the in-service front. The training may consist of periodic short courses promoted by State universities with the encouragement of the State agency. The Institute of Government in North Carolina is a good example of the successful combination of training courses, conferences, and manuals in an organization in which all levels of government participate in both financial and functional programs.

Explanation of the Complexities of the Bond Market

The State agency can perform a service for local finance officers by explaining to them the complexities of the bond market touched upon in Chapter 1. As indicated there, the variations in bidding practices, in particular, contain a number of pitfalls for the uninitiated. The State can help local governments cope with them by keeping current with new developments in bidding practice, conducting research into the different ways bids are submitted, and providing guidelines for evaluating alternative bids.

States can be helpful to their local governments in other aspects of bond marketing. These include such items as the length of the maturity schedule, whether or not to include a call feature,

and whether to negotiate a sale with a local bank or investment banker or to invite bids on the open market. Since interest rates often fluctuate widely (even from week to week), a well-informed State advisory agency could provide some guidance as to the timing of a bond issue, guidance which could result in savings to the borrowing government.

Chapter 3

SUPPLEMENTAL TECHNICAL ASSISTANCE

The basic plan sketched in Chapter 2 can be viewed as setting the metes and bounds for minimum State involvement in technical assistance to local debt management. Local circumstances may well suggest two additional steps some States may want to take to help local governments with their borrowing problems:

1. Advisory review of proposed local bond issues
2. Optional State sale of local bonds

Local communities in depressed areas have special need for assistance that could be provided by a State advisory review service, and the remoteness of many small communities from the money market underscores the advantage to be derived from State sale of their bonds. Other communities may also benefit from these two types of assistance.

Neither of these proposed activities involves coercion on the part of the State. Thus, while a State agency reviewing a proposed bond issue may feel strongly that the project is ill-conceived and possibly unnecessary, or that the issuing government may be borrowing beyond its fiscal capacity, it is not authorized, under these plans, to disallow the bond issue. On the other hand, it is anticipated that a strongly negative report will certainly have a deterrent effect on the borrowing plans of a local government that has come to the State for advice.

ADVISORY REVIEW OF PROPOSED LOCAL BOND ISSUES

By undertaking to review proposed bond issues of local governments the State agency would provide some of the services available also from private bond counsel and financial consultants. In some respects it could go farther. For example, investment counsel is concerned primarily with the ability of a borrower to service the debt, not necessarily with the need for the project. The amount of return investors are willing to accept for their money is based

upon their judgment as to the degree of risk they are willing to take when they lend money to a particular local government. The State's interest might well extend beyond this. If a local jurisdiction proposes to finance entirely from its own resources a facility for which assistance from the State or Federal governments is in prospect under prescribed conditions, a State agency reviewing the proposed bond issue would be in a position to share this information with local officials and to suggest appropriate revision of the financing plans.

In essence, State review of local debt offerings involves three elements: (a) the need for the capital improvement; (b) the fiscal ability of the local government to pay debt and other costs; and (c) the legality of the bond issue. A possible by-product of this review is an appraisal of the fees the local government pays for the services it hires in connection with the bond issue.

As indicated previously, the review contemplated here is not mandatory; a State undertaking this kind of technical assistance would provide it only upon local request. On the other hand, if the availability of the service is to be of any value, local governments should be fully apprised of its benefits and encouraged to make use of it. A number of the technical assistance measures discussed in Chapter 2 could be used by the State agency to apprise local governments as to the advantages of the advisory review procedure. The preliminary financial reports would provide an especially useful vehicle for this purpose, as would in-service training sessions, and periodic bulletins and newsletters. To keep abreast of current and pending local bond issues, the State agency should be authorized to require that local governments notify it at an early stage of any proposed debt financing, whether or not they are submitting the proposal for advisory review.

Advisory review of local bond issues would be initiated by a local notification report to the State agency that a local bond issue is contemplated. State and local consultation is essential in the early fluid stage of consideration, before local plans have finally crystallized. The local notification report would consist essentially of parts A and B--identification and legal authority--in the listing of "Tests for Advisory Review of Bond Issues," on pages 48 and 49. These tests, it must be emphasized, are not cast in the form of a local schedule or report, nor do the tests comprise all the questions that communities or bond investors might desire to consider. The outlined tests are for advice as to the acceptability of the issue from the State standpoint, while reserving other considerations to the community and to the bond investors for their decision.

TEST FOR ADVISORY REVIEW OF BOND ISSUES

A. Identification

1. Proposed bond issue as to amount, term, and schedule showing annual debt service until maturity;
2. Explanation of purpose and need for project to be financed, describing in physical terms the nature of the project;
3. Future capital budget correlating receipts by source with disbursements by purpose; and
4. Extent and use of physical plant (immediately past and future) for selected functions for which data are available and relationship to the proposed project (for example, school buildings and enrollment, classified highway or street mileage, sewerage system, and water or other revenue-producing facility by plant capacity and consumption).

B. Legal Authority

1. Recitation of relevant statutory or charter provisions and proposed bond ordinance; and
2. Legal borrowing capacity under debt limit setting forth total amount permitted, gross debt, subtractions for allowed deductions, net limited debt, and unused margin.

C. Past and Current Ability to Pay Debt and Other Costs

1. Percentage distribution of revenue of general, utility, and other funds separately to show relative reliance on property taxes, local nonproperty tax revenues, and intergovernmental revenues;
2. Percentage distribution of expenditure, by fund, to show relative functional claims on revenue and bond proceeds;
3. Debt service as a percentage of revenue of the fund from which the proposed bond issue would be payable; 1/

1/ Revenue here is defined as gross revenue, including service charges. Excluded from general revenue and classified in separate funds would be not only utility services but also sewerage and any other general function if financed from service charges.

TEST FOR ADVISORY REVIEW OF BOND ISSUES -- Continued.

4. Property tax rates of prospective borrower and of overlying units; 2/ expressed also as rates adjusted to full valuation;
5. Net general obligations and general debt service as percentages of full valuation, and total and overlying general debt as a percentage of full valuation;
6. Property tax collections as a percentage of tax levies and cumulative amount of tax delinquencies;
7. Net general obligations and general debt service as percentages of total and overlying property tax levies;
8. Net interest costs of recent bond issues, separately computed for general obligation and for revenue bonds, compared with similar costs of comparable borrowers and of high-quality local bonds; and
9. Gross earnings of utility or self-financing enterprises, classified charges against earnings, and surplus or deficit; extent of transfers to general funds or of transfers from general funds to enterprise funds.

D. Future Ability to Pay Debt and Other Costs

1. Size of additional debt service for proposed bond issue, spread over the term of the issue, and total debt service for prospective issue and outstanding obligations;
2. Extent of additional capital improvements, likely new debt, and use of current revenue for improvements;
3. Increase in property tax rates, tax levies, and in utility or service rates resulting from proposed bond issue, and forecast of total revenue of general, utility, and other relevant funds; and
4. Adequacy of future utility or enterprise earnings to cover debt service and other charges, providing an extra margin for assurance of payments.

2/ The word "overlying" is used throughout the outline to connote, wherever called for, "underlying" or "coterminous."

Tests under sections C and D of the list of "Tests for Advisory Review of Bond Issues"--past, current, and future ability to pay debt and other costs--could usually be determined by the State agency from the brief notification report and from debt and general financial reports, audits, and other file data in the State office, described in chapter 2. The outline is concerned with general obligation or full faith and credit bonds, and revenue or self-financing bonds, which account for most of local long-term obligations. Tailoring of the outline would be advisable for limited tax liability bonds (secured, for example, by utility or cigarette taxes), and for bonds pledging a double security (for example, special assessment bonds carrying a pledge of full faith and credit). Without specifying the years for which the prospective issue would be evaluated, the list of tests assumes a suitable number of years, whether three, six, or other number, for which trend lines are desirable.

Review of the Need for the Proposed Project

While the necessity and expediency of bond issues is essentially a question for local formulation and decision, the State agency can assist the local government officials in two important ways. First, the agency can help the local officials place their various long-term construction requirements on an orderly priority basis by helping them prepare a capital budget, described in chapter 2.

The second step involves cooperation between the State technical assistance agency and the State functional departments maintaining detailed records of local functions with which they are concerned. These are, for example, the State departments of education for local school plants, highway departments for rural highways and urban streets, and health departments for water and sewerage systems. Each bond issue involving one of these functions can and should be cleared through the appropriate department for comment and advice.

Review of Fiscal Capacity to Service the Debt

The major problem in appraising local capacity is the measurement of economic ability against which to relate debt and other fiscal loads. Per capita debt is useful in comparing the size of debts for a series of years or among localities, provided the comparison is sufficiently close to decennial censuses or dependable intercensal population estimates are available, but debt size must be related to the economic base if fiscal loads are to be measured.

Personal income of residents is valuable as an all-inclusive measure of ability, but dependable income statistics below the State level are prepared in only a few States. While not necessarily a measure of fiscal ability, retail sales form a useful indicator of the level of economic activity.

In the outline on pages 48 and 49, the suggested tests carry out in economic terms the implications of the legal character of liability by relating general obligation bonds to property valuations, both assessed and full value, and revenue bonds for self-financing projects to the revenue generated by the projects. Estimated full valuation, though suspect in some States and small areas, is becoming more reliable as the number and sophistication of assessment ratio studies increase. Neither full valuation nor any other measure is to be accepted as conclusive because the validity of the evaluation depends upon the use of a series of tests.

Debt service as a percentage of revenue--a measure proposed at times as a substitute for the customary debt limit--illustrates the danger of placing exclusive reliance on one test. The debt service percentage has value in indicating the weight of debt in current budgets, but two identical amounts of debt service may represent widely different percentages of revenue--in one case a small per cent of large total revenue, but constituting a heavy fiscal load, and in the other case a large per cent of a small total revenue, but one that can be comfortably paid. Accordingly, not only the debt service or debt load must be measured but also the total tax load of the prospective borrower as well as of all taxes levied by the borrower and overlying governments.

Interrelations among tests are especially helpful in appraisals of proposed bond issues. Thus, net general obligations and general debt service as percentages of total and overlying tax levies measure the debt load in relation to the total property taxation on variable valuations. Similarly, the percentage distributions of revenue by source and of expenditure by purpose, together with debt measures, afford a view of the entire fiscal structure.

After initially differentiating between legal liability, according to sources of funds to pay debt, a bond issue evaluation should paradoxically move in the opposite direction by bridging the gap between general obligation and revenue bonds. The legal distinction between these two types, as is often pointed out, may conceal underlying economic similarities or interrelations that

affect ability to pay. Dedication of revenue from self-financing projects or from nonproperty taxes to pay revenue bonds or limited tax liability bonds may so reduce general revenue as to require replacement revenue that increases fiscal loads. The extent of utility transfers to general funds or from general to enterprise funds may be crucial in reviewing a bond issue. Therefore, utility statements are germane to the appraisal of general obligations, and selected general obligation tests are relevant to the appraisal of revenue bonds.

Legal Review

The practice of requiring a State legal review of proposed local bond issues originated in some States to correct local laxity or abuses in the local incurrence of debt, or to assure compliance with legal provisions authorizing debt incurrence and requiring debt retirement, or to provide an incontestable State record of legally issued obligations. Thus, the Massachusetts State certification of town and district notes, dating from 1910 and 1915 acts, was to assure taxpayers and investors of the authenticity and legality of notes that might be doubtful.^{1/} When the question arose as to extension of certification to town and city bonds, however, the State turned to annual and special reports to establish a reliable record of local obligations.

Of the 15 States specified in table 4 as providing some type of State legal review, the attorney-general's office is the examining agency in seven. The review agency calls upon the Attorney General regularly to clear legal questions in Michigan, and on occasion in Louisiana. A legal officer, the State's Bond Attorney, is appointed by the State Supreme Court to check and validate Mississippi local bonds. This officer constitutes the only separate agency of any State to perform only the legal review function. In the remaining five States, the review agency is the State Local Finance Officer in Kentucky, the Director of Municipal Accounts in Massachusetts, the State Auditor in Missouri and Nebraska, and the Bureau of Municipal Affairs (Department of Internal Affairs) in Pennsylvania.

^{1/} Royal S. Van De Woestyne, State Control of Local Finance in Massachusetts, Harvard University Press (Cambridge: 1935), pp. 112-119.

TABLE 4. - STATE LEGAL REVIEW OF LOCAL GOVERNMENT BORROWINGS

State	State review agency	Type of local obligations	Volume of issues in 1960 or 1961	
			Amount	Number
Arizona	Attorney General	General obligations	n.a.	Few <u>1/</u>
Kansas <u>2/</u>	Attorney General	Bonds and notes	\$ 84,485,592	402
Kentucky	Local Finance Office, Department of Finance	County general obligations	2,599,000	8
Louisiana	Bond and Tax Board <u>3/</u>	Bonds and notes	218,192,672	330
Massachusetts	Director of Accounts	Town and district notes	99,508,322	249
Michigan	Municipal Finance Commission <u>4/</u>	Bonds and notes	358,937,206	529
Mississippi	Bond Attorney	Bonds	n.a.	357 <u>1/</u>
Missouri <u>2/</u>	Auditor	Bonds <u>5/</u>	99,761,500 <u>6/</u>	264 <u>6/</u>
Nebraska <u>2/</u>	Auditor	Bonds <u>7/</u>	58,573,000	214
New Mexico	Attorney General	Bonds	n.a.	37
Oklahoma	Attorney General	Bonds	n.a.	n.a.
Pennsylvania	Bureau of Municipal Affairs	Selected local general obligations <u>8/</u>	68,156,100	132
Texas <u>2/</u>	Attorney General	Bonds	411,874,370	591
West Virginia	Attorney General	General obligations	n.a.	60
Wisconsin	Attorney General	Local general obligations	n.a.	Few <u>1/</u>

n.a. - data not available.

1/ Optional local request for State review. 2/ Legal review a phase of the process of registering local bonds with the State Auditor or Comptroller. 3/ Bond issues at times referred to Attorney General. 4/ Bond issues cleared as to legality by Attorney General. 5/ Excludes counties of the first class and cities and school districts having populations over 300,000. 6/ For 1960 and 1961. 7/ Comprises bonds of second class cities, villages, precincts, school districts, and specified types of special districts. Data on volume covers all bonds registered. 8/ Excludes general obligations of cities and school districts of Philadelphia and Pittsburgh, and of the city of Scranton.

Source: Statutes and letters from and conferences with officials of listed States.

By custom, the State legal review does not substitute for examinations and opinions by private bond attorneys, and investors rely on private opinions before purchasing the obligations of local governments. Where there is a State legal review, however, the work of local officials and private attorneys is reduced by the ironing out of "bugs" in local borrowing proceedings. Some savings to the borrowing governments should result.

Fees Connected with Borrowing

A State agency providing the kinds of technical assistance described in chapter 2 and, in addition, reviewing local bond issues, would build up a fund of information by which it could evaluate the fees paid in connection with local bond issues. Several types of fees are involved--engineering and architectural, bond counsel, financial consultant, and printing. As it gains experience in reviewing local bond issues, the State agency will be able to detect instances of exorbitant fees concerning which it can alert the borrowing government.

The Michigan Municipal Finance Commission, whose responsibility in the local debt field extends beyond technical assistance to the coercive type of supervision, was concerned with the variations it detected in the fees reported to it by local government borrowers. The broad supervisory authority of the Commission includes the power to deny a local bond issue, under an opinion of the State Attorney General, if it considers the fees to be exorbitant. ^{1/} Even without the coercive powers of the Michigan Municipal Finance Commission, a State advisory review procedure should request information on the contractual fees connected with proposed bond issues as an integral part of the review process. Disclosure of such fees would of itself serve as a deterrent to sharp practice.

Reporting the Findings of a State Advisory Review

State review of proposed local bond issues would result in one of three findings--favorable, questionable, and unfavorable. Undoubtedly, in the majority of cases the finding would be "favorable." In this case, the complete body of findings of the State agency would be submitted to the local governing officials as an informational report. All other bond issues would be subject to more intensive study, particularly as to the community's economic base and the nature

^{1/} Opinion No. 2678, Attorney General of Michigan, December 26, 1956.

of the pending issue. In many cases, especially when the finding was "questionable," a modification of the bond issue in consultation with the local officials would change the finding to "favorable." A change in the term of the issue, a different graduation of bond maturities, a rewording of the bond covenant, or a reduction in amount illustrate the various modifications that could make the pending issue acceptable.

For the remaining issues, for which restudy and modification failed to eliminate objectionable features, the complete body of State findings would be submitted as "unfavorable" or with the suggestion that the bond issue be deferred until a later time or recast in a new plan. Decision on such issues would, of course, be up to the local governing body, perhaps in conjunction with a referendum. In any action taken by the local government, full publicity should be given to the State review findings.

OPTIONAL STATE SALE OF LOCAL BONDS

Once a State has established an organization and procedures to assist local governments with their debt problems, it may find it practicable to go one step further--to market bond offerings for local governments. Two States are now doing this successfully--North Carolina since 1931, and Virginia since 1950.

Aside from the possible economies accruing to local governments from the State sale of local bonds, the bond buyers themselves profit from it. A Virginia bond man, Walter W. Craigie, has made a strong case for the centralized sale, particularly of the offerings of small communities. ^{1/} He pointed out the inconvenience of appearing at a town council meeting in the evening when sealed bids often are opened, often in a town that is not easily accessible by public transportation and at a considerable distance from the bond man's home office. By contrast, the capital city is reached easily, the opening of bids is the only business at hand, and sales are held at a convenient hour. Commenting on the operations of the North Carolina and Virginia Commissions, Craigie writes:

^{1/} Walter W. Craigie, "'Centralize!' - A Call for Streamlined Bidding," The Daily Bond Buyer, Special Conference Issue No. 1, May 28, 1962. (Mr. Craigie is Senior Partner of F. W. Craigie and Co., Richmond, Virginia.)

...the operations of these commissions have been so eminently satisfactory that many bond houses (which formerly spent a lot of money in the form of manpower as well as traveling expenses in covering sales in person) now merely mail their bids and get the results by telephone. This is a high tribute to the integrity of both bodies. 1/

North Carolina started selling local bonds in 1931 when it set up a supervisory agency, the Local Government Commission, to cope with widespread defaults of local obligations. Consistent with the stringent regulatory aspects of the North Carolina system, the State sale of local bonds is mandatory.

The background resulting in the Virginia plan, instituted in 1950, differed from the North Carolina crisis of 1931. Virginia's conservative borrowing practices had spared that State of local defaults during the Depression. The question in 1950 was what technical assistance the State could render local governments without imposing either uniform State control upon local debt incurrence or mandatory State sale of local securities. The answer was to place the two primary services performed by the Virginia Commission on an advisory and optional basis. The first service consists of advice to the locality "on all matters relating to the planning, preparation, and marketing of (proposed) bonds," and the second is assistance to the locality "in the sale of such bonds." 2/

The Virginia Commission serves as a sales agent for the local government requesting the service. Bids are opened and bond contracts are awarded at the Commission's office, with one or more members of the local government present. To carry out the sale function, however, the previous steps of study and planning, review of bonds, and preparation and circularization of debt prospectuses among possible buyers are generally performed with the assistance of the State Auditor on behalf of the State Commission on Local Debt. Thus, the State sale of securities requires a series of prior steps to obtain an expression of local opinion, to develop well-conceived plans

1/ Ibid., p. 39.

2/ Virginia Code, Section 15-666.16. The State Commission on Local Debt is composed of the State Auditor of Public Accounts, the State Treasurer, the State Tax Commissioner, and two other members appointed by the Governor.

for improvements and bond issues, and to take maximum advantage of competitive bidding in an informed bond market. ^{1/}

These preliminary steps include conferences of State and local officials, a series of audit reports, supplementary data furnished by the local officials, local improvement plans prepared by independent architects and engineers, and legal opinions of private bond counsel. Financial information is derived primarily from audit reports. The State Auditor's staff annually audits the 96 counties and some of the 35 cities. If audits have not been completed for the towns, most of which are under 10,000 in population, a representative of the Auditor visits the towns and assembles the records. To up-date the audits, current information regarding key questions, such as valuations, tax rates, and levies, is assembled.

The process leading to sale usually involves a sequence of steps, the first of which is a preliminary conference of the State Auditor with the local officials. The project plans are outlined locally, and the Auditor indicates the procedures to be followed both in preparing and in marketing bonds.

Having helped the local government to assess the feasibility of the project (to the extent appropriate), and having guided it through the necessary preliminary steps, the State Auditor undertakes to prepare a report, outlining the financial and economic condition of the community, for the national bond rating agencies. Submission of this report is expedited to permit a rating of the prospective issue well in advance of the sale.

The next step is vital to an economical sale--the preparation and printing of the prospectus. The prospectus is distributed by the State Auditor among some 250 to 300 investment dealers in order to stimulate as extensive bidding as possible. An accompanying step is the advertisement in two newspaper editions of a notice of sale at least two weeks before the sale.

Next, all sealed bids offering to purchase the bonds are opened in the State Commission's office in the presence of the bidders and interested parties. The best bid is immediately accepted or rejected. Finally, the local government awards the construction contract.

^{1/} Conference with J. Gordon Bennett, Virginia State Auditor of Public Accounts, May 10, 1961; letters from Mr. Bennett June 5, 1961 and April 6, 1962; and address by Mr. Bennett before the Michigan Municipal Debt Seminar, May 8, 1962.

Table 5 records the bond issues sold by the State Commission, according to the number and amount of issues, from July 1, 1952 to June 30, 1964. The extent of the sales must be understood, of course, in the light of the locally optional request for State sale. The State services have been especially helpful to the smaller communities unacquainted with legal debt requirements and bond marketing. Though the larger communities at times avail themselves of the State services, a substantial share of their bond sales is directly to bond dealers.

Local governments have profited from the activities of the Virginia Commission on Local Debt in the form of better prices for their bonds and some savings in financial consultants' fees. The centralization of local bond sales intensifies the competition for the offerings, and the availability of detailed information on local finances tends to upgrade credit ratings.

Because of its optional character, the Virginia system of State sales is preferable to the North Carolina mandatory system. Many of the larger local governments can afford the necessary technical services and believe they can do a better marketing job than the State. Furthermore, local finance officers "feel highly complimented when 15 or 20 representatives of nationally known municipal houses journey to their localities to submit bids." ^{1/} Even when the State sells bonds for a local government at its request, the local officials do not abdicate their own responsibilities. In the final analysis, they make the key decisions--the kind and size of project the community needs, the amount of money to be borrowed, and whether the community can afford the project. The State merely helps with the technical aspects of marketing the bonds.

^{1/} Walter W. Craigie, op. cit., p. 39.

TABLE 5. - LOCAL BOND ISSUES SOLD BY THE VIRGINIA STATE COMMISSION
ON LOCAL DEBT, JULY 1, 1952 to JUNE 30, 1964
(dollar amounts in thousands)

Fiscal Year	Total		Counties		Cities		Towns	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount
1953	7	\$ 7,245	4	\$ 4,030	2	\$ 1,875	1	\$ 1,340
1954	16	23,455	10	20,730	4	2,450	2	275
1955	13	11,454	6	4,378	6	6,951	1	125
1956	8	10,315	3	6,050	3	3,750	2	515
1957	17	18,931	9	13,125	5	5,106	3	700
1958	15	15,908	5	6,220	6	8,683	4	1,005
1959	18	28,094	9	19,309	6	6,475	3	2,310
1960	9	9,242	1	130	4	7,937	4	1,175
1961	15	22,976	10	18,531	2	3,100	3	1,345
1962	15	32,975	8	21,620	5	10,665	2	690
1963	18	36,160	12	27,645	4	7,725	2	790
1964	16	45,045	9	34,200	5	10,270	2	575
Total	167	261,800	86	175,968	52	74,987	29	10,845

Source: Virginia State Commission on Local Debt.

APPENDICES

APPENDIX A

Recommendations from Advisory Commission Report, State Constitutional and Statutory Restrictions on Local Government Debt (A-10; September 1961)

1. Local governments should be granted maximum powers with respect to local government indebtedness. The Commission recommends that State provisions with respect to local government indebtedness take cognizance of all forms of local borrowing and debt. The intended application of such State provisions should be made explicit, and they should be designed to facilitate - rather than hamper - intelligent choice among suitable alternative forms of borrowing by the local governments concerned. This objective is most likely to be served if any conditions that attach legally to the borrowing power of an individual local government apply uniformly - or subject only to specifically defined exceptions - to any type of long-term debt it can incur.
2. The Commission recommends that authority to issue bonds should be legally vested in the governing bodies of local governments, subject to a permissive referendum only, on petition, and with participation in any such referendum available to all eligible local voters and the results determined - except under unusual circumstances - by a simple majority vote on the question.
3. The Commission recommends the repeal of constitutional and statutory provisions limiting local government debt or debt service by reference to the local base for property taxation.
4. The Commission recommends that the States study and consider measures to regulate long-term borrowing of local governments by reference to the net interest cost of prospective bond issues in relation to the currently prevailing interest rate on high quality municipal securities.
5. The Commission recommends that States make available technical and advisory assistance to local governments with regard to the issuance of long-term debt; and that the State agency responsible for this function be empowered to prescribe the minimum content of official statements prepared by local governments in connection with their issuance of long-term debt in order to provide prospective investors with data needed to evaluate the security offerings.

APPENDIX B

Information Suggested for Inclusion in a
Bond Prospectus by the Investment Bankers Association
(Excerpt from Fundamentals of Municipal Bonds, I.B.A.,
January 1963, pp. 44-50)

REPORT ON FINANCES - MUNICIPAL GENERAL OBLIGATION BONDS

Municipality or political subdivision _____
County _____ State _____

Form of Government (Commission, Mayor-Council, Manager, etc.) _____
Fiscal year begins _____
U. S. Census 19__ : _____ State Census 19__ : _____ Present Estimate: _____
Has this issuer defaulted on any debt obligation since 1930? _____
If so, give full particulars in a separate statement.

Part 1. Property Valuation (as of _____ 19__)

	Current Year			Previous Year	
	Assessed	Actual	Ratio of assessed to actual value	Assessed	Actual
1. Real estate	\$ _____	\$ _____	_____%	\$ _____	\$ _____
2. Personal property	_____	_____	_____	_____	_____
3. Public utility	_____	_____	_____	_____	_____
4. Other (specify) _____	_____	_____	_____	_____	_____

Part 2. Bonded Debt and Related Information (as of _____ 19__)

	Amount	Sinking Funds
1. General obligations (not listed below)	\$ _____	\$ _____
2. Special assessments secured also by general tax	_____	_____
3. Utility and public enterprise debt secured also by general tax:		
(a) Water	_____	_____
(b) Sewer	_____	_____
(c) Light and Power	_____	_____
(d) Other (specify) _____	_____	_____
Total General Obligation Bonds	_____	_____
4. Special assessments only	_____	_____
5. Utility and public enterprise revenue only:*		
(a) Water	_____	_____
(b) Sewer	_____	_____
(c) Light and Power	_____	_____
(d) Other (specify) _____	_____	_____
Total Other Than General Obligations	_____	_____

*For utility and other public enterprise revenue bonds, please submit separate reports on report form for municipal revenue bonds.

- 6. Legal debt limit of this issuer? ____% of (describe base) _____; \$ _____
- 7. Debt outstanding chargeable to debt limit? \$ _____ Unused borrowing margin? \$ _____
- 8. Bonds authorized but not issued: Purpose _____ Amount \$ _____
- 9. Are utility and public enterprise bonds reported in item 3 fully supported by earnings of the facilities? ____ If not, what proportion of general taxes was necessary for debt service on such bonds in the last fiscal year? _____
- 10. Total general obligation bonds outstanding year ago? \$ _____ Two years ago? \$ _____
- 11. Amount of refunding bonds issued within last two years for the following purposes:
 - (a) To refund maturing bonds \$ _____ Maturities _____
 - (b) To refund callable bonds \$ _____ Maturities _____

Part 3. Overlapping Debt

That Part of Debt of Overlapping Entities (School or Special Districts, Counties, etc.) Payable by Taxes Levied in this Municipality or Political Subdivision

Name of Overlapping Entity	Debt		Gross Debt Less Sinking Fund	This Issuer's Share
	Limit	%		
_____	_____	_____	\$ _____	\$ _____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____

Part 4. Unfunded Debt Outstanding

	<u>Amount</u>	<u>Due</u>
1. Tax Anticipation Notes	\$ _____	_____
2. Delinquent Tax Notes	\$ _____	_____
3. Bond Anticipation Notes	\$ _____	_____
4. Bank Loans	\$ _____	_____
5. Warrants	\$ _____	_____
6. Judgments	\$ _____	_____
7. Unpaid Bills 60 Days Past Due	\$ _____	_____
8. Miscellaneous Items	\$ _____	_____
Total	\$ _____	_____
9. Unfunded Debt One Year Ago \$ _____; Two Years Ago \$ _____		

Part 5. Composition of Sinking Funds

1. Cash on hand or in banks	\$ _____
2. United States Government securities	\$ _____
3. Bonds of this municipality	\$ _____
4. Bonds of states and other municipalities	\$ _____
5. Other investments (specify nature)	\$ _____
Total	\$ _____
6. Amount of Term Bonds for Which Sinking Funds Are Required	\$ _____

**Part 6. Debt Service Requirements For Next Five Years
(For principal, interest and sinking fund installments)**

<u>Authorized Source of Payment</u>	<u>Fiscal Year Beginning</u>				
	19__	19__	19__	19__	19__
1. General Taxation	\$ _____	\$ _____	\$ _____	\$ _____	\$ _____
2. Special Assessments and General Taxation	\$ _____	\$ _____	\$ _____	\$ _____	\$ _____
3. Utility Revenues and General Taxation	\$ _____	\$ _____	\$ _____	\$ _____	\$ _____
4. Special Assessments Only	\$ _____	\$ _____	\$ _____	\$ _____	\$ _____
5. Utility Revenues Only	\$ _____	\$ _____	\$ _____	\$ _____	\$ _____

Part 7. Comparative Statement of Operating Revenues and Expenditures.

Do not include municipally operated utilities or public enterprises, unless surplus revenues therefrom are transferred to general fund (in revenues) or debt service on general obligations issued therefor are paid from general fund (in expenditures).

	<u>Fiscal Year Beginning</u>		
	19__	19__	19__
1. Cash Balance at beginning of year	\$ _____	\$ _____	\$ _____
2. Revenues:			
(a) Proceeds from notes and bonds	\$ _____	\$ _____	\$ _____
(b) From ad valorem taxes	\$ _____	\$ _____	\$ _____
(c) From other taxes	\$ _____	\$ _____	\$ _____
(d) From federal or state aid	\$ _____	\$ _____	\$ _____
(e) From other sources	\$ _____	\$ _____	\$ _____
Total Revenues	\$ _____	\$ _____	\$ _____
3. Expenditures:			
(a) Government operating expenses	\$ _____	\$ _____	\$ _____
(b) Expenditures from bond proceeds	\$ _____	\$ _____	\$ _____
(c) Bond principal	\$ _____	\$ _____	\$ _____
(d) Bond interest	\$ _____	\$ _____	\$ _____
(e) Sinking Funds	\$ _____	\$ _____	\$ _____
(f) All other purposes	\$ _____	\$ _____	\$ _____
Total Expenditures	\$ _____	\$ _____	\$ _____
4. Cash Balance at end of year	\$ _____	\$ _____	\$ _____

Part 8. Tax Data

(a) **Tax Collection Report - Ad Valorem or General Property Tax**
 For last 3 years. For tax or fiscal year ending _____
 Omit levies of other entities and special assessments.

	Amount of Levy By This Issuer	Uncollected at End of Year	Uncollected Latest Available Date	Delinquent Taxes From Prior Years Collected During Year
19__	\$ _____	\$ _____	\$ _____	\$ _____
19__	\$ _____	\$ _____	\$ _____	\$ _____
19__	\$ _____	\$ _____	\$ _____	\$ _____

(b) **Total Current Levy**

For tax or fiscal year beginning _____
 Include levies of other entities which are part of general property tax

	Amount Levied	Rate Per \$100 of Assessed Value*
This Issuer	\$ _____	\$ _____
School	\$ _____	\$ _____
County	\$ _____	\$ _____
State	\$ _____	\$ _____
Other _____	\$ _____	\$ _____
Total	\$ _____	\$ _____

*If any property included in your taxable assessed valuation is taxed at rate different from real estate, specify _____

(c) **General Tax Information**

- Taxes for fiscal year are due: _____ Became delinquent: _____
- If payable in installments give particulars _____
- Discounts for prepayment and when applied? _____
- Specific practice for delinquency? _____
- Explain in detail any modifications of practice during the past two years _____
- How are uncollected taxes handled?
 - Anticipated as revenue in next year's budget? If yes, what percentage? _____
 - Turned over to other governing bodies? If yes, when? _____
 - Sale of tax certificates? If yes, when? _____
 - Other methods _____
- Has tax sale period been extended in last two years? If yes, explain _____
- Accumulated total of uncollected taxes for fiscal years prior to those reported above \$ _____
- Are tax title liens included in uncollected tax totals above? _____
 How much? \$ _____
- Total tax title liens owned by municipality (years 19__ to 19__ inclusive) \$ _____
- Is there a tax rate limit? How Much? _____ Statutory or Constitutional? _____
- Do tax rate limits apply to debt service? If yes, what are the limits? _____
- Do you levy taxes in excess of actual requirements to provide margin against delinquencies? Yes ___ No ___
 If yes, what ratio? Current year? ___%; Previous year? ___%; 2 years ago? _____

Part 9. Supplementary Information

Please furnish in a separate statement information regarding the location and economic background of the issuer, the general character of industries and transportation facilities in the area, and any other pertinent data or comments. If additional space is needed to report fully the information requested in this form, please attach separate sheets with appropriate cross references.

Signed _____

Official Title _____

Date _____

REPORT ON FINANCES - MUNICIPAL REVENUE BONDS

Name of Issuer _____
 Type of Facility _____

Part I - General Information and Protective Features

1. Population of area served _____ (U.S. Census 19__)
2. Amount of bonds authorized \$ _____ Amount issued \$ _____
3. Date of issue _____
4. Maturities (state below):

Amount	Rate	Date	Amount	Rate	Date	Amount	Rate	Date
\$ _____	_____	_____	\$ _____	_____	_____	\$ _____	_____	_____
_____	_____	_____	_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____	_____	_____	_____

5. Call provisions, if any. If noncallable prior to maturity please so state.

6. What is purpose of issue? _____

7. If purpose is for new construction or development give engineer's estimate of gross and net revenue expected over next five years:
 Gross \$ _____ \$ _____ \$ _____ \$ _____ \$ _____
 Net \$ _____ \$ _____ \$ _____ \$ _____ \$ _____
8. What is peak requirement for interest and principal or sinking fund? _____
 What year is peak reached? _____
9. Amount of outstanding revenue or other bonds which have a claim on the revenue from this project \$ _____
 (a) Are there securities having a claim junior to this issue? Yes No If "Yes", show
 Amount \$ _____ Maturity _____ Peak debt service requirements \$ _____
 (b) Are there securities having a claim equal to this issue? Yes No If "Yes", show
 Amount \$ _____ Maturity _____ Peak debt service requirements \$ _____
 (c) Are there securities having a claim prior to this issue? Yes No If "Yes", show
 Amount \$ _____ Maturity _____ Peak debt service requirements \$ _____
10. Schedule of rates or charges for services of the facility. Date effective _____
 (Give particulars in a separate statement)

11. Controlling covenants of the bond indenture, authorizing resolution or act. Attach separate statement, if necessary.

(a) In what order are the revenues disposed of (flow of funds)? _____

(b) What reserve funds are provided for and what are the requirements of each? What is the amount in each at present?

Name of reserve fund	Requirements	Present Amount
_____	_____	\$ _____
_____	_____	_____
_____	_____	_____
_____	_____	_____

How are reserve funds invested? _____

(c) What is the covenant or legal requirement respecting the rates to be charged for the services rendered? _____

(d) What are the provisions for issuance of additional bonds? _____

(e) Is the preparation of an annual budget required? Yes ___ No ___
If "Yes", is a public hearing provided for? Yes ___ No ___

(f) Is issuer required to make public statement regularly re earnings? Yes ___ No ___
If "Yes", how often? _____

(g) What insurance is required:
Type _____ Amount \$ _____
Type _____ Amount \$ _____
Type _____ Amount \$ _____

(h) Is there a requirement that consulting engineers be retained? Yes ___ No ___
If "Yes", for what purpose and how often? _____

(i) Do bondholders have the benefit of a mortgage? Yes ___ No ___

12. Name of corporate trustee, if any _____

13. Name of consulting engineer(s), if any _____

14. Name of the attorney(s) approving the legality of the issue _____

15. Has the facility defaulted during the past 20 years for a period of 60 days or more in the payment of either principal or interest of any of its bonds or notes? Yes ___ No ___
If "Yes", give full particulars in a separate statement, including terms of settlement.

16. Is there a competitive system in operation? Yes ___ No ___ If "Yes", give in a separate statement the system's name, location and extent of its operations.

17. Are any contributions to be made to or received from any political body? Yes ___ No ___
If "Yes", give details _____

18. Please furnish in a separate statement information regarding the location and economic background of the issuer, and the general character of industries and transportation facilities in the area served. Attach a statement of any other pertinent data or comments.

Part 2 - Current Data on Revenues, Expenditures and Financial Condition

	<u>Fiscal Year</u> <u>ended _____</u>	<u>Same period</u> <u>1 year ago</u>	<u>Same period</u> <u>2 years ago</u>
1. Operating Revenue	\$ _____	\$ _____	\$ _____
2. Nonoperating Revenue	_____	_____	_____
3. Total Gross Revenue	\$ _____	\$ _____	\$ _____
4. Expenditures:			
(a) For Operation	_____	_____	_____
(b) For Maintenance	_____	_____	_____
5. Other charges, if any, against Gross Revenue	_____	_____	_____
6. Net Income available for debt service	_____	_____	_____
7. Interest paid on bonded debt	_____	_____	_____
8. Principal paid on bonded debt	_____	_____	_____
(a) Matured	_____	_____	_____
(b) Called	_____	_____	_____
9. Other charges against Net Income (specify various funds) *			
(a) _____	_____	_____	_____
(b) _____	_____	_____	_____
(c) _____	_____	_____	_____
(d) _____	_____	_____	_____
10. Amount available for retirement of debt by call	_____	_____	_____
11. Surplus (state to what uses surplus has been or may be put)	_____	_____	_____
12. Total amount of bonds issued (original & subsequent)	_____	_____	_____
13. Bonded debt at end of period (also show below)	_____	_____	_____
(a) Bank loans at end of period	_____	_____	_____
(b) Other unfunded debt at end of period	_____	_____	_____
14. Principal & Interest on bonded debt next fiscal year	_____	_____	_____
15. Present book value of plant or facility, equipment and fixed assets, after depreciation	_____	_____	_____
16. Attach copy of latest balance sheet, as of _____			
Are there any contingent liabilities not shown in the balance sheet? Yes ___ No ___			
If "Yes", explain _____			
Name and address of auditor preparing the annual audit _____			
Is the auditor an independent auditor? Yes ___ No ___			
*What method of depreciation is used? _____			
*What disposition is made of revenue in these funds? _____			

Part 3 - Special Information on Particular Types of Revenue Bonds

<u>(A) For electric revenue bonds only:</u>	<u>Fiscal Year</u> <u>ended _____</u>	<u>Same period</u> <u>1 year ago</u>	<u>Same period</u> <u>2 years ago</u>
1. KWH's generated	_____	_____	_____
2. KWH's purchased	_____	_____	_____
3. KWH's sold	_____	_____	_____
4. Number of customer:			
at end of period:			
Residential	_____	_____	_____
Industrial	_____	_____	_____
Commercial	_____	_____	_____
All Others	_____	_____	_____
5. KWH's consumed per customer:			
Residential:	_____	_____	_____
Industrial	_____	_____	_____
Commercial	_____	_____	_____
All Others	_____	_____	_____

(B) For water or sewer revenue bonds only:

		Fiscal Year ended _____	Same period 1 year ago	Same period 2 years ago
1. Estimated average daily water supply (in gallons)		_____	_____	_____
2. Average daily water consumption (in gallons)		_____	_____	_____
3. Water storage capacity (in gallons)		_____	_____	_____
4. Number of customers at end of period:	Residential	_____	_____	_____
	Commercial	_____	_____	_____
	Industrial	_____	_____	_____
	All Others	_____	_____	_____
5. Gallons water consumed per customer:	Residential	_____	_____	_____
	Commercial	_____	_____	_____
	Industrial	_____	_____	_____
	All Others	_____	_____	_____
6. Is sewer service charge based on amount of water metered? Yes ___ No ___ If not what is the base? _____				
7. Does the sewer charge appear on water bill? Yes ___ No ___				
8. May water and sewer charges be paid separately? Yes ___ No ___ If "Yes", explain _____				
9. Does the law provide that past due bills become a lien on the property? _____				
10. Does the law provide that water may be cut off if bills are not paid? _____				
11. What is the source of water supply? _____				

(C) For toll bridge or highway:

	12 Months ended _____		Same period last year		Same period 2 years ago	
	Vehicles	Revenue	Vehicles	Revenue	Vehicles	Revenue
1. <u>Traffic:</u>						
Passenger Cars	_____	\$ _____	_____	\$ _____	_____	\$ _____
Trucks and Busses	_____	_____	_____	_____	_____	_____
2. Other income (specify) _____						

Signed _____

Official Title _____

Date _____

APPENDIX C

Suggested Legislation for State Assistance to Local Debt Management

√Title should conform to state requirements. The following is a suggestion: "An act to provide state assistance and regulation regarding local government debt offerings."√

(Be it enacted, etc.)

TITLE I

TECHNICAL AND ADVISORY ASSISTANCE

1 Section 1. Purpose. It is the intent of this Title to
2 facilitate, through state technical and advisory assistance,
3 the marketing of local government bonds and other long-term
4 obligations at the lowest possible net interest cost.

1 Section 2. Definitions. (a) "Local government" means a
2 county, city, village, town, township, school district, and
3 other special-purpose district, authority, or public
4 corporation within the state and authorized by the state to
5 issue bonds and other long-term obligations.

6 (b) "Governing body" means the body or board charged with
7 exercising the legislative authority of a local government.

8 (c) "Agency" means √insert name of the appropriate agency

9 of state government¹.

10 (d) "Chief financial officer" means the comptroller,
11 treasurer, director of finance or other local government
12 official charged with managing the fiscal affairs of a local
13 government¹.

14 (e) "Bonds" means debt payable more than one year after
15 date of issue or incurrence, issued pursuant to the laws
16 authorizing local government borrowing.

1 Section 3. Authorization for State Technical and Advisory
2 Assistance. The Agency is authorized and directed to
3 provide technical and advisory assistance regarding the
4 issuance of long-term debt to those local governments whose
5 governing bodies request such assistance. Such assistance
6 shall include, but need not be limited to, (a) advice on the
7 marketing of bonds by local governments, (b) advisory review
8 of proposed local government debt issues, including the
9 rendering of opinions as to their legality, (c) conduct of
10 training courses in debt management for local financial
11 officers, and (d) promotion of the use by local governments of

¹ The agency charged with this function will vary from state to state. Normally it will be the agency, if any, that is charged generally with concern or oversight regarding local government debt or that provides general services or assistance to local governments or, in the absence of such agency, the agency that is responsible for the marketing of the state's obligations.

12 such tools for sound financial management as adequate systems
13 of budgeting, accounting, auditing, and reporting.

1 Section 4. Advisory Review of Proposed Local Government
2 Debt Issues. At the request of the governing body of any
3 local government, the [Agency] is authorized to review a
4 proposed debt issue and to render an advisory opinion based
5 upon the facts concerning the proposed issue. Any request for
6 an advisory review shall be submitted to the [Agency] in such
7 form and with such information as the [Agency] may require.

1 Section 5. State Sale of Local Government Security
2 Offerings. At the request of the governing body of any
3 local government, the [Agency] is authorized to market such
4 local government's security offerings by preparing bond issues
5 for sale, advertising for sealed bids, receiving bids at its
6 offices, and making the award to the bidder that offers the
7 most favorable terms. The [Agency] may, at its discretion,
8 offer for concurrent sale the bonds of several local govern-
9 ments. State sale of a local security offering under this
10 section shall in no way imply state guarantee of such debt
11 issue.

1 Section 6. Powers and Duties of the [Agency]. The [Agency]
2 shall have the following powers and duties:

3 (a) To require such reports from local governments as will
4 enable it adequately to provide the technical and advisory
5 assistance authorized by this Act. The reports shall provide
6 the necessary information for a complete file on local govern-
7 ment debt, which shall be kept open for public inspection at
8 Agency offices.

9 (b) To encourage, conduct or participate in training
10 courses in debt and general fiscal management and procedures
11 and practices for the benefit of local officials, and in
12 connection therewith, to cooperate with associations of public
13 officials, business and professional organizations, university
14 faculties, or other specialists.

15 (c) To conduct studies in debt management, including ways
16 and means of appraising the terms of alternative bids. The
17 Agency may employ expert consultants to assist in such
18 studies.

19 (d) To employ or contract for the services of personnel
20 necessary to carry out the provisions of this Act, subject to
21 the provisions of statutory citation.

22 (e) All departments, divisions, boards, bureaus, commis-
23 sions, or other agencies of the state government shall
24 provide such assistance and information as, not inconsistent
25 with law, the Agency may require to enable it to carry out

26 its duties under this Act.

27 (f) To compile and publish annually a report on its
28 technical assistance and advisory activities. Such report
29 shall include detailed information on local government long-
30 term debt issued and retired during the previous calendar
31 or fiscal year and outstanding at the close of the previous
32 calendar or fiscal year, and such additional statistical
33 data on local government finances that are obtained by the
34 Agency pursuant to par. (a) of this section.

TITLE II

STANDARDS FOR OFFICIAL STATEMENTS ON LOCAL DEBT OFFERINGS

1 Section 1. Purpose. It is the intent of this Title to
2 facilitate the marketing of bonds by local governments by
3 providing minimum standards as to the kinds of information to
4 be included in advertising notices and sales prospectuses.

1 Section 2. Authorization. The Agency is authorized and
2 directed to prepare regulations concerning the minimum content
3 of the notice of sale advertisements and prospectuses required
4 by statutory citation. Regulations as to the content of
5 such notices and prospectuses may make an appropriate

6 differentiation among types of bond issues and types of local
7 government.

1 Section 3. Notice of Sale Advertisement. The notice of
2 sale advertisement shall set forth the purpose of the bond
3 issue, principal amount of the bond issue, designation of
4 type of bond issue according to the authorizing statute, date
5 of issue, the method of bond repayment, showing the denomina-
6 tions and maturities offered for sale, the basis of bidding
7 and award of the bonds, the date, hour, and place that bids
8 will be opened, the name of the chief financial officer who
9 will furnish additional information about the issuing local
10 government or the bond sale, and any other appropriate
11 information, in accordance with the regulations prepared by
12 the Agency.

1 Section 4. Prospectus. The prospectus shall, in general:
2 (1) report the past, current, and estimates as to the future
3 finances of the bond-issuing local government; (2) include
4 selected information concerning the financial administration
5 and organization of the bond-issuing local government; (3)
6 contain selected information concerning the economic and
7 social characteristics of the community in which the issuing
8 local government is located, including such data as will

9 permit investors and other interested parties to appraise the
10 ability of the borrowing local government to assume the
11 obligation; and (4) any other appropriate information, in
12 accordance with the regulations prepared by the Agency.

1 Section 5. Inclusion of Additional Information. The chief
2 financial officer may, at his discretion, include information
3 in the notice of sale advertisement and in the prospectus in
4 addition to that specified as the minimum content in regula-
5 tions issued by the Agency.

1 Section 6. Bid Forms. The Agency is authorized and
2 directed to prepare and supply standard bid forms to be used
3 by local governments in securing bids from prospective
4 purchasers.

TITLE III

SEPARABILITY AND EFFECTIVE DATE

1 Section 1. Insert separability clause.

1 Section 2. Insert effective date.

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