

MUNICIPAL OBLIGATIONS IN NEVADA

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This article will provide an overview of bonds, notes and other documents evidencing a promise to repay money borrowed (herein “bonds” and other “obligations”) from the state of Nevada and local governments (referred to as “issuers” of those bonds and other obligations). With few exceptions, the borrowed money, obtained from bonds and other obligations issued by governments, is used to finance activities or facilities owned, operated or used by the issuer or another government for its own purposes, including public infrastructure, such as schools, fire stations, parks, libraries, highways, water and sewer infrastructure and other types of municipal facilities. Government financing of projects owned by non-government entities, which are usually financed by economic development revenue bonds issued by counties, cities and the Department of Business and Industry, is beyond the scope of this article.



Dillon’s Rule

Dillon’s rule provides “It is a general and undisputed proposition of law that a municipal corporation possesses and can exercise the following powers, and no others: First, those granted in express words; second, those necessarily or fairly implied in, or incident to, the powers expressly granted; third, those essential to the accomplishment of the declared objects and purposes of the corporation – not simply convenient, but indispensable.”¹ Dillon’s rule was adopted by the Nevada Supreme Court in 1937,² and consequently applies to the issuance of bonds and other obligations by governments in Nevada. (For more on Dillon’s Rule, see the article on page 6.)

Types of Obligation Under Nevada Law

Bonds and other obligations under Nevada law include bonds, notes, debentures, warrants, and lease or installment purchase agreements. Lease and installment purchase agreements are frequently sold to several investors in the form of “certificates of participation.”

Local governments are prohibited from issuing bonds or other evidences of borrowing obligations to pay operating expenses, except in a few rare circumstances.³ Consequently, the proceeds of bonds and other obligations in Nevada are generally used to finance capital expenditures.



General Obligation Bonds and Other General Obligations

General obligation bonds and other general obligations are secured by the full faith, credit and taxing power of the issuer. All general obligation bonds in Nevada are “limited tax” obligations. Nevada Revised Statute (NRS) 361.453 limits the property tax that can be levied for all purposes by all overlapping entities to \$3.64 per \$100 of assessed valuation, with a few limited exceptions. Further, Article 10, Section 2 of the Nevada Constitution limits all overlapping property taxes to \$5 per \$100 of assessed valuation, with no exceptions. Generally, to issue general obligations that are expected to be paid with property taxes, an election is required. NRS 350.020(1) (2011).

In addition, general obligations in Nevada may be issued as “limited” limited tax obligations. These are obligations containing a pledge of the full faith and credit of the government issuing the obligations, including the government’s taxing power, but for which the issuer does not have the authority to levy a specific additional property tax for the repayment of the obligations; however, the issuer can use its operating property tax and non-property tax revenues to pay these obligations. The most frequent example of a “limited” limited tax general

obligation is a medium-term obligation authorized by NRS 350.087 to 350.095. An election is not required to issue medium term obligations.

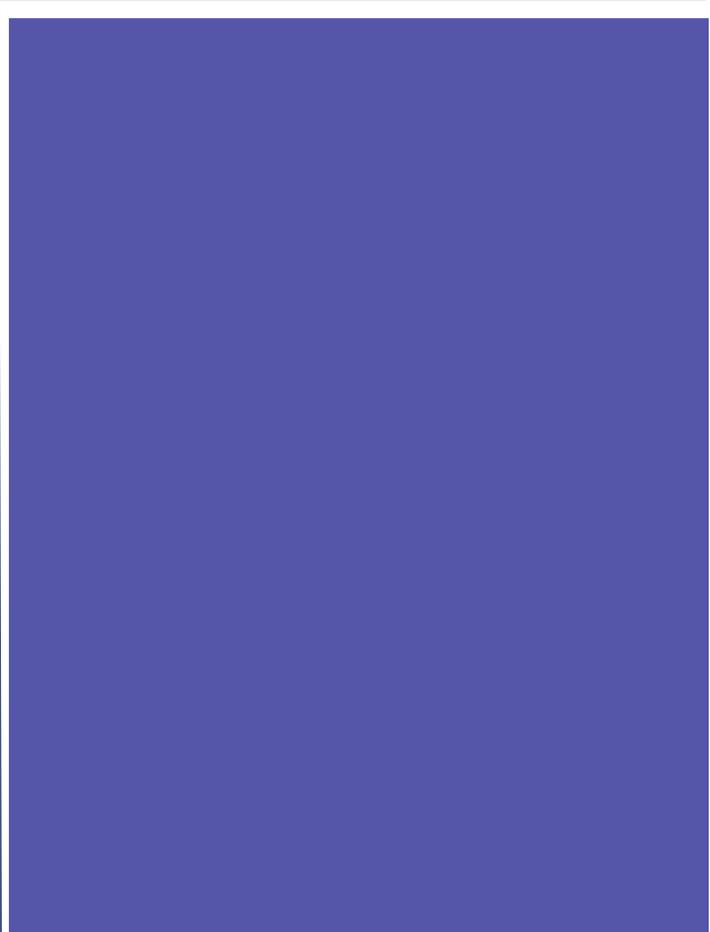
Revenue Bonds and Other Revenue Obligations

Revenue bonds and other revenue obligations (sometimes called “special” obligations) are obligations secured by a designated special fund, consisting of monies from a designated source, not derived from property taxes in the case of local governments, and not derived from any state taxes in the case of the state. Frequently, revenue obligations are secured by an enterprise’s revenues (e.g., an airport revenue bond is secured by, and payable from, airport revenues) and local government revenue bonds can be secured by excise taxes (e.g., room tax revenue bonds are issued by convention authorities and some counties and cities secured by and payable from room taxes). An election is not required to issue revenue obligations.

Revenue-Backed General Obligations

Revenue-backed general obligations, sometimes called “double barrel obligations,” are obligations with a pledge of the full faith and credit and taxing power of the issuer, which are also secured by, and are expected to be paid from, a designated revenue source other than property taxes. Although the property taxing power is pledged to the bonds, the only time the property taxing power would be used for the obligations would be in

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the event that the revenues were insufficient, due to an emergency or unexpected situation. Double barrel general obligations do not require an election unless 5 percent of the registered voters petition for an election. NRS 350.020(3) (2011).

Installment Purchase or Lease Purchase Agreements

Installment purchase or lease purchase agreements are each a type of obligation that does not require an election as long as the government's obligation to pay the installment or lease payments is extinguished by a failure to appropriate money for that purpose. The holder of such an obligation has no enforceable right to receive money from the issuer if the governing body decides not to appropriate funds to pay the installment or lease payment in any year. Usually, in the event the government fails to appropriate the lender, or if the lease or installment purchase agreement is distributed among investors by issuing certificates of participation, the trustee for the certificate holders will receive ownership of the facility that was financed by the obligation. *See* NRS 350.800 (2011).

Special Assessment Obligations

Special assessment obligations are securities payable from "special" assessments levied against property within a specific part of a government's territory that is "specially" benefited by installation of the improvements financed with the bonds. Common projects financed by this type of bond include street paving projects and water main projects. A government may pave several blocks of street and assess property owners, whose property fronts on the street, for the cost of the paving, and issue bonds or other obligations payable from the assessments. An election is not required. *See* NRS 271 (2011).

Redevelopment Obligations

Redevelopment obligations are generally issued as special obligations, and no election is required. In Nevada, these obligations are payable from property taxes allocated to a redevelopment area: they are generally the property taxes within the boundaries of the redevelopment area, resulting from increases in assessed valuation, occurring after formation of the redevelopment area. *See* NRS 279 (2011).

CONSTITUTIONAL AND STATUTORY DEBT LIMITS AND IMPAIRMENT OF BONDS

Debt Limits

The Nevada Constitution, Article 9, Section 3, limits the aggregate amount of debt of Nevada, to 2 percent of the assessed valuation of the state, with certain exceptions. Local governments have debt limits imposed by statute.⁴



Impairment of Contract

If the state has authorized a particular type of borrowing and the state, or a local government, has borrowed money pursuant to that authority, the state cannot change the laws in a manner that will "impair" the contract with the bondholders.⁵ The U.S. Supreme Court has interpreted this clause in the Constitution strictly, and held actions by states that diminished bondholder security to be as invalid as an impairment of the contract between the issuer and the bondholder.⁶

FEDERAL TAX LAWS

Sections 103 and 141 to 150 of the Internal Revenue Code of 1986, provide a complicated set of rules that must be followed in order for a governmental obligation to bear interest exempt from federal income taxation. These rules are generally aimed at preventing the tax exemption from benefiting private businesses, and an issuer from earning "arbitrage profits," (i.e., profits from borrowing at a tax-exempt interest rate and investing the borrowed monies in higher interest rate taxable bonds). In the last 10 years, the Internal Revenue Service has been operating an aggressive program of auditing government bonds for compliance with these tax-exempt bond rules.

FEDERAL SECURITIES LAWS

Securities and Exchange Commission Rule (SEC) 10b-5 prohibits making false or misleading statements, or omitting statements that should be made, in documents offering to sell securities, and other communications made in connection with the sale or purchase of a security, including a government bond. For government bonds, the offering document is usually called the "official statement." Early in 1996, the SEC sanctioned the members of the board of supervisors of Orange County, California for violating this rule in connection with bond and note offerings prior to that county's bankruptcy. Later in the same year, Maricopa County, Arizona's largest county, was sanctioned for not disclosing all material information in its official statements. Recent SEC actions have sanctioned Miami, New Jersey and Illinois. ■

- 1 Dillon, *Municipal Corporations*, Sec 237 (5th ed. 1911), quoted in *Runnow v. City of Las Vegas*, 65 P.2d 133, 136 (1937).
- 2 *Runnow v. City of Las Vegas*, 65 P.2d 133, 136 (1937).
- 3 NRS 354.6256 (2011).
- 4 A county's debt limit is 10 percent of assessed valuation of the taxable property of the county. NRS 244A.059 (2011). A city's debt limit for incorporated cities is set forth in NRS 266.600(4) (2011) as 30 percent of the assessed valuation of the taxable property within such city. Chartered cities have debt limits as set forth in their charters. A school district's debt limit is 15 percent of the assessed valuation of taxable property, excluding motor vehicles, situated within the district. NRS 387.400 (2011). A general improvement district's debt limit is 50 percent of the total of the assessed valuation of taxable property (excluding motor vehicles) situated within such district. NRS 318.277 (2011).
- 5 U.S. Const. art. 1, Sec. 10; Nev. Const. Art. 1, Sec. 15.
- 6 See *U.S. Trust Company of New York v. New Jersey* 431 U.S. 1 (1977).

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