



TEXAS MUNICIPAL LEAGUE
Empowering Texas cities to serve their citizens

President **David Rutledge**, Mayor, Bridge City
Executive Director **Bennett Sandlin**

April 27, 2023

The Honorable Paul Bettencourt
Chairman, Senate Local Government Committee
Texas Senate
P.O. Box 12068
Austin, TX 78768-2068

Dear Chairman Bettencourt:

I am writing on behalf of the Texas Municipal League to express our opposition to **S.B. 977**. The bill would redefine “debt” for purposes of calculating a property tax rate to exclude any debt not approved at an election. This would include debt instruments like certificates of obligations (COs) along with other obligations like tax notes, lease-purchase and other equipment financing debt, and even refunding bonds. By requiring these debt instruments to be funded from maintenance and operations revenue despite fitting any conventional definition of “debt,” S.B. 977 would largely eliminate the use of these instruments altogether since maintenance and operations revenue is capped and necessary for operating costs subject to significant cost drivers. This would not only hinder the development of necessary water, sewer, electric, transportation, and broadband infrastructure across the state, but force taxpayers to pay more in the process.

According to the Bond Review Board, the majority of outstanding city debt in Texas is not tax-supported debt but instead is considered “self-supporting” debt.¹ This means most city debt is ultimately issued for water, sewer, and other revenue producing projects that are paid by utility revenues, and not property taxes. Cities have a couple of different debt options to pay for utility system work – revenue bonds and COs. Both debt obligations require attorney general approval, neither requires an upfront election, but COs are issued with more notice and the potential for voter approval, unlike revenue bonds. And, most importantly, COs can be issued in a significantly more cost-efficient way for city residents.

Cities commonly issue COs in lieu of revenue bonds to finance needed utility construction and upgrades. The reason for this is pretty straightforward – COs typically cost much less to issue than a revenue bond. COs issued by cities are generally repaid with revenues from city utility systems instead of property taxes. However, the city’s property tax base can serve as “credit support” in a CO, thus reducing borrowing costs and interest rates. Overall, the use of self-supporting COs by Texas cities has saved taxpayers hundreds of millions of dollars as compared to other debt

¹ See BRB’s 2022 *Local Government Annual Report*:
<http://www.brb.state.tx.us/pub/lgs/fy2022/2022LocalARFinal.pdf>.

instruments.² By effectively eliminating the use of COs, S.B. 977 would have the unintended effect of costing city taxpayers and ratepayers significantly more money, with no discernable public benefit.

It should also be noted that COs are regularly used by Texas cities to evidence loans under state and federal financial assistance programs. For instance, cities commonly issue COs to the state to draw down funding from the Texas Water Development Board for various critical water infrastructure project needs. In doing so, cities obtain reduced interest rates and financial assistance from the state. The state agency receives stronger credit ratings in return due to the underlying property tax pledge supporting the CO. S.B. 977 would significantly discourage the use of COs by a city to draw down needed state and federal infrastructure funding. This means that at the same time the Texas Legislature potentially invests billions of dollars into water infrastructure projects this session, S.B. 977 would drastically limit cities' ability to access the new funding.

The Texas Legislature has enacted several substantive and process reforms relating to the issuance of COs and other non-voter-approved debt instruments in recent years. In 2015, the legislature passed H.B. 1378 to prohibit the issuance of a CO within three years of a failed bond election on the same project. Four years later in 2019, the legislature passed H.B. 477, which significantly enhanced the notice required when a CO is issued, from requiring additional published and internet notice to increasing the amount of time voters may circulate a petition to call an election on a CO issuance. Last session, H.B. 1869 passed to eliminate some of the rare but controversial uses of COs and other non-voter-approved debt instruments. And this session, this committee has passed out legislation that would put additional safeguards on the use of COs and tax notes. We ask this committee to let recent reforms continue to work, while rejecting attempts to effectively eliminate the use of COs and other obligations as S.B. 977 proposes to do.

For the reasons stated above, the League opposes S.B. 977.

Sincerely,



Monty Wynn
Director, Grassroots and Legislative Services
Texas Municipal League

² Masterson, Drew. "What if Certificates of Obligation Go Away." *Texas Town and City*, March 20, 2021, https://www.tml.org/DocumentCenter/View/2540/032021_TTC.