SUBJECT: Limiting political subdivisions' ability to issue capital appreciation bonds

COMMITTEE: Investments and Financial Services — committee substitute recommended

VOTE: 6 ayes — Parker, Longoria, Capriglione, Flynn, Landgraf, Stephenson

0 nays

1 absent — Pickett

WITNESSES: *Subcommittee on Bond Indebtedness:*
For — Peggy Venable, Americans for Prosperity; James Quintero, Texas Public Policy Foundation; Cobby Caputo (*Registered, but did not testify*: Kelley Shannon, Freedom of Information Foundation of Texas)

Against — None

On — Johnny Hill, Fast Growth Schools Coalition; Keith Bryant, Lubbock-Cooper ISD, Fast Growth Schools Coalition; Rogelio Rodriguez, the Finance Industry; (*Registered, but did not testify*: James Hernandez, Harris County, Harris County Toll Road Authority)

BACKGROUND: Capital appreciation bonds are a form of bond that does not pay interest until its maturity date. Because political subdivisions are not required to pay out monthly or quarterly interest payments, capital appreciation bonds sometimes are used to raise funds when a political subdivision could not otherwise afford to issue bonds. Some school districts issue capital appreciation bonds when they are near the state-mandated limit for how much tax revenue may be spent for bond maintenance.

DIGEST: CSHB 114 would place certain limitations and requirements on political subdivisions that issued capital appreciation bonds. The bill would limit the amount of capital appreciation bonds a political subdivision could issue to no more than 25 percent of the subdivision's total bond indebtedness at the time of issuance. To determine its total amount of bond indebtedness, the political subdivision would be required to include the amount of principal and interest that must be paid on outstanding bonds until maturity.

Political subdivisions would be prohibited from issuing capital appreciation bonds that were secured by ad valorem taxes unless:

- the bonds had a scheduled maturity date of not more than 25 years after the date of issuance;
- the governing body of a political subdivision had received a written estimate of the projected tax impact of the bond;
- the governing body had received a written estimate of the amount in principal, interest, and fees to be paid before maturity;
- the governing body had determined in writing whether any personal or financial relationship existed between any governing members of the political subdivision and professionals associated with the bond issuance; and
- the governing body had displayed on its website the amount of the proposed bond, the length of maturity, projects to be financed with the bond, and other pertinent information.

These restrictions would not apply to the issuance of refunding bonds under Government Code, ch. 1207 or capital appreciation bonds issued for transportation projects.

Political subdivisions would be prohibited from using capital appreciation bonds to purchase maintenance items or transportation-related items, such as buses. Political subdivisions could only spend any unused surplus on uses that had been identified on the bond’s website. Unused bond proceeds could be spent for another use if the political subdivision first held a successful election to repurpose the bond proceeds.

Political subdivisions would be prohibited from extending the maturity date of an issued capital appreciation bond in most cases, including through the issuance of refunding bonds that extend the maturity date. A political subdivision would be able to extend the maturity date if the extension decreased the total amount of projected principal and interest that the subdivision would have to pay until maturity or if the political subdivision was a school district and the Texas Education Agency certified that the solvency of the permanent school fund's bond guarantee program would be threatened without the extension.

The bill would take effect September 1, 2015, and would not affect the validity of capital appreciation bonds issued before that date.