

# ALTERNATIVES FOR FINANCING SCHOOL PERMANENT IMPROVEMENTS

Presented by:  
Rebecca C. Princehorn, Esq.



**Bricker & Eckler**  
ATTORNEYS AT LAW

**BRICKER & ECKLER LLP**  
PUBLIC SECTOR GROUP

**100 South Third Street  
Columbus, Ohio 43215  
(614) 227-2300**

**1375 East Ninth Street  
Suite 1500  
Cleveland, OH 44114  
(216) 523-5405**

**9277 Centre Pointe Drive  
Suite 100  
West Chester, OH 45069  
(513) 870-6700**

**[www.bricker.com](http://www.bricker.com)**

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## 1.1 Introduction.

Ohio school districts, unlike Ohio municipalities, do not have "home rule" power. Therefore, school districts are entirely subject to the control of the state legislature, both as to the powers and duties of board members and the way in which they can finance permanent improvements.

The Ohio Revised Code ("O.R.C.") strictly limits the ways in which school districts can borrow money. Contrary to popular belief, there are several ways to finance permanent improvements for school districts. Selecting the appropriate alternative, however, will require an analysis of its legal and practical constraints. This chapter discusses those legal and practical constraints in summary form, first in the area of state law and, second, in the area of federal securities and tax law.

### 1.1.1 Glossary of Basic Terms.

"Arbitrage" -- The profit that results from borrowing money at low, tax-exempt interest rates and using it to purchase high yield, taxable investments, such as certificates of deposit or U.S. Treasury Bills. Arbitrage is very strictly regulated by federal tax laws.

"Bonds" -- Long term obligations to repay money, usually one (1) to thirty (30) years.

"Bond Anticipation Notes" -- Notes issued to provide temporary project financing, on the expectation that the notes will be repaid with the proceeds of the bonds when issued.

"Bond Counsel" -- A law firm that specializes in the preparation of bond proceedings and renders its legal opinion on the validity and tax exempt status of the bonds.

"Bond Registrar" -- Usually the trust department of a major bank, the registrar maintains records of the names and addresses of all bond holders and is responsible for mailing out interest checks and redeeming the bonds at maturity.

"CFAP" -- Classroom Facilities Assistance Program of the Commission.

"Commission" -- The Ohio School Facilities Commission.

"Controlling Board" -- The appropriations entity of the State of Ohio.

"Debt Service" -- The total amount of principal and interest payable during each year a bond issue is outstanding.

"Direct Debt Limitations" -- O.R.C. Section 133.06 generally limits the amount of general obligation bonded indebtedness of school districts in two ways: unvoted bonds may not exceed 1/10 of 1% of the school district's tax valuation [9/10 of 1% (Section 133.06(G), O.R.C.) or 1% (Section 3313.372, O.R.C., if security is property tax based) for qualifying energy

projects], and the total of voted plus unvoted bonds may not exceed 9% of the school district's tax valuation. Exceptions include: (1) the school district qualifying as a "special needs" district; and (2) the school district participating in a Commission program and its financing is entirely for Commission-required local effort, Sections 133.06(I), 3318.052, and 3318.44, O.R.C.

"Dominant County" -- The county that contains the highest amount of the tax valuation of the school district or that otherwise has jurisdiction in practice over and customarily handles property tax matters relating to the school district.

"ELPP" -- Expedited Local Partnership Program of the Commission.

"General Obligation" -- Also referred to as "G.O.", this term describes bonds which are secured by a pledge of the property taxing power. The same as "full faith and credit" bonds.

"Joint Vocational School District" means a joint vocational school district created pursuant to Section 3311.18, O.R.C.

"Limited Tax" -- Bonds which are supported by an unvoted property tax, thus inside the ten-mill limit.

"Municipal Bond Insurance" -- Insurance policies sold by one of several companies ("MBIA", "AMBAC", "FGIC", etc.) which guarantee the repayment of all principal and interest on the bonds. This allows the bond issuer to obtain the highest possible rating on the bonds and results in lower interest costs.

"Notes" -- Short term obligations to repay money, usually one (1) year or less.

"Official Statement" -- The disclosure document, usually in printed, booklet format, which contains detailed information regarding the school district and its finances. Used in the note/bond sale process and often required by the federal securities laws.

"Permanent Improvement" -- Any capital asset with a useful life, as determined by the school treasurer, of five (5) years or more.

"Rating Agency" -- One of three companies (Moody's Investors Service, Inc., Standard & Poor's Rating Group, and Fitch Ratings) that evaluate the creditworthiness of bonds and notes and issue ratings (such as AA, A+, Baa, etc.).

"Rebate" -- The payment of arbitrage profits to the federal government. Under some circumstances, arbitrage profits must be paid to the federal government in order to preserve the tax exempt status of bonds or notes.

"Ten Mill Limit" -- A constitutional and statutory ceiling on the total amount of unvoted property taxes that can be levied by the school district, county, and other taxing authorities (city, township, etc.) acting together. Also known as the "indirect" debt limitation.

"Underwriter" -- The company, usually a bank or investment banker, that purchases bonds and notes for re-sale to its customers.

"Uniform Public Securities Law" -- Chapter 133 of the O.R.C., the primary statute covering notes and bonds.

"Unlimited Tax Bonds" -- Bonds which are supported by a voted property tax, thus outside the ten-mill limit.

## 1.2 Permanent Improvement Levies.

School districts can finance permanent improvements by obtaining voter approval for a permanent improvement levy<sup>1</sup>. This alternative to a voted bond issue is generally appropriate where the school district is planning a series of relatively small permanent improvement projects each year for several years. A bond issue, by contrast, is generally called for when the district is contemplating a single, large scale project.

### 1.2.1 Statutory Authority for the Permanent Improvement Levy.

.1 Traditional permanent improvement levy. Section 5705.21, O.R.C., permits a school district to submit to its voters the question of whether to levy a permanent improvement property tax to construct or acquire a specific permanent improvement; class of improvements that could be included in a single bond issue; community centers; general, permanent improvements; or education technology.<sup>2</sup> Infrastructure improvements pursuant to an Ohio School Facilities Commission program require special mention. The levy may be for a fixed period of time (from one (1) to five (5) years) or for a continuing period of time (if it is a levy for general, permanent improvements). School districts with a time-limited permanent improvement levy may renew or replace that levy for a continuing period of time. The procedural steps to place a permanent improvement levy on the ballot are as follows:

- a. Resolution of Necessity - The board of education declares the necessity of the levy; specifies whether additional, renewal or replacement; specifies O.R.C. section authorizing submission; specifies mills and dollar amount per hundred dollars of valuation; and specifies election date. Two-thirds vote of all members of the board of education required.

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<sup>1</sup> Many school districts that have reached the twenty (20) mill floor of Section 319.301, O.R.C., have unvoted permanent improvement levies. It should also be noted that proceeds from a voted permanent improvement levy may be substituted for general fund revenues for purposes of the three percent (3%) (or another percentage designated by the State Auditor) of general fund set-aside for permanent improvements and maintenance (acquisition, replacement, enhancement, maintenance or repair of permanent improvements) required under Section 3315.18, O.R.C., unless exempted due to fiscal status.

<sup>2</sup>"Education technology" is defined in the statute as including, but not limited to, computer hardware, equipment, materials, and accessories, equipment used for two-way audio or video, and software.

- b. County Auditor's certification - The county auditor determines the total current tax valuation and the dollar amount of revenue the levy will generate in the first year of collection and shall certify those amounts to the school district. The county auditor shall issue such certification to the school district within ten (10) days after receiving the school district's resolution requesting such certification.
- c. Resolution to Proceed - The board of education determines to proceed with the levy; reiterates foregoing information; provides ballot form, including specific language if the tax is to be imposed in the current tax year, i.e. "commencing in \_\_\_\_\_, first due in calendar year \_\_\_\_\_. Two-thirds vote of all members of the board of education required.

All of the foregoing documents must be certified to the board of elections of the school district's dominant county no later than ninety (90) days before the election.

.2 Combined operating and permanent improvement levy. Section 5705.217, O.R.C., permits a school district to submit to its voters a combined property tax for current operating expenses and permanent improvements. The election proceedings for such tax levy are similar to those of a traditional permanent improvement levy, except it must apportion the annual rate of the tax between current operating expenses and permanent improvements. Such apportionment is not required to be the same for each year of the tax, but the respective portions of the rate actually levied each year are limited by the apportionment. The levy may be for a fixed period of time (from one (1) to five (5) years) or for a continuing period of time if the tax is for current operating expenses or for general, ongoing permanent improvements.

### 1.2.2 Borrowing Authority for the Permanent Improvement Levy.

Sections 5705.21 and 5705.217, O.R.C., provide that, following approval of the levy,<sup>1</sup> the board of education may issue tax anticipation notes for up to fifty percent (50%) of the levy's proceeds to be collected over the life of the levy (if a continuing levy, fifty percent (50%) of the levy's proceeds over a maximum of ten (10) years). After this money is spent, a board of education having a traditional permanent improvement levy for a fixed term or a continuing

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<sup>1</sup>Before a school district is able to complete any financing involving a vote of the people, a permanent improvement levy note issue, or a voted bond or bond anticipation note issue, it must wait for a certificate of result of election from the board of elections of the school district's dominant county and for the contest period to run. Section 3505.32, O.R.C., provides that the board of elections must begin the canvass of election returns within 11 to 15 days of the date of the election and complete such canvass by the 21<sup>st</sup> day after the date of the election. Section 3515.09, O.R.C., provides that the contest period runs 15 days after the results of the election have been announced by the proper authority. Consequently, for scheduling purposes, it is generally advisable to plan on closing the bond or note issue no sooner than 30 days after the election. Section 3501.01, O.R.C., provides that election dates generally are the first Tuesday after the first Monday in February, May, August and November, except for presidential election years in which the May election is moved to the first Tuesday after the first Monday in March and no February election is held (unless otherwise authorized by a municipal or county charter).

period may apply to the Superintendent of Public Instruction under Section 5705.216, O.R.C., for permission to issue additional tax anticipation notes for an amount equaling the balance of the taxes to be collected less the amount of money required to pay the principal and interest on the first issue of notes.

### 1.2.3 Debt Limitations Applicable to Permanent Improvement Levy Notes.

Notes issued in anticipation of a permanent improvement levy are "exempt debt" pursuant to Section 133.04(B)(2), O.R.C., for purposes of the two "direct debt" limitations<sup>1</sup> and are exempt from the "indirect" or ten-mill limitation.<sup>2</sup>

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<sup>1</sup>Section 133.06, O.R.C., imposes direct debt limitations on unvoted and combined unvoted and voted general obligation net indebtedness, with certain exceptions. The unvoted limitation is generally one-tenth of one percent (1/10 of 1%) of the school district's tax valuation, with exceptions for: (i) financings for energy conservation projects (nine-tenths of one percent (9/10 of 1%) - Section 133.06(G), O.R.C., and one percent (1%) - Section 3313.372, O.R.C., if secured by property tax revenues); and (ii) paying all or a portion of the school district's local share under a Commission program (in excess of one percent (1%) - Sections 3318.052, O.R.C., if secured by property or income tax revenues and Section 3318.44, O.R.C., if secured by property tax revenues). The combined unvoted and voted limitation is nine percent (9%) of the school district's tax valuation, with an exception for school districts that qualify as "special needs" districts or if the school district is participating in a Commission program and its local effort exclusively for that program exceeds nine percent (9%). "Special needs" districts can exceed the nine percent (9%) limit by an amount based on either nine percent (9%) of the growth in taxable value over the past five (5) years or nine percent (9%) of the projected growth in taxable value over the next ten (10) years. Special notes: (1) the voted general obligation debt of a school district library counts against the school district's nine percent (9%) debt limitation under Section 3375.43, O.R.C.; (2) "net indebtedness" does not include some types of obligations, including those issued to acquire buses or certain lease-purchase arrangements; and (3) debt secured by receipts of a school district pursuant to economic development arrangements under Sections 5709.43 and 5709.82, O.R.C., are exempt from the one-tenth of one percent (1/10 of 1%) and nine-tenths of one percent (9/10 of 1%) limitation, with the consent of the Superintendent of Public Instruction.

<sup>2</sup>The Ohio Constitution, Article XII, Section 2 imposes the ten-mill limitation, which provides that no property can be taxed in excess of one-percent (1%), based on its true value, absent a vote of the people. Section 5705.02, O.R.C., imposes a limitation of ten (10) mills (equivalent to one percent (1%)) on each dollar of tax valuation. The ten mill limitation applies to the aggregate of taxes which may be levied for payment of debt service (principal and interest) on unvoted general obligations issued by all overlapping subdivisions taxing the same property. The ten mill limitation is distinguished from the ten (10) mills of unvoted taxes which are in fact levied, collected, and distributed each year, for general fund purposes, to the various overlapping political subdivisions according to a fixed statutory formula. To the extent that a political subdivision actually levies and collects the millage earmarked for debt service on unvoted notes or bonds, tax revenues that would otherwise have gone into its general fund are reduced. If such debt service levies exceed the millage collectible for general fund purposes, general fund revenues payable to the other overlapping political subdivisions will, to the extent of the excess, be reduced proportionally.

#### 1.2.4 Practical Considerations Regarding Permanent Improvement Levy Notes.

Complications caused by the requirement of two note issues make this alternative less efficient from a planning and flow of funds standpoint. Also, the permanent improvement levy is subject to the reduction factor, Section 319.301, O.R.C. (House Bill 920), and may only be submitted to the voters three times during any calendar year, Section 5705.214, O.R.C.

#### 1.3 Voted Debt.

By far the most common method of financing major school permanent improvement projects is through the use of voted bonds. Section 133.18(A), O.R.C., permits taxing authorities, including school district boards of education, to seek voter approval of general obligation bonds and of the levy of property taxes outside the ten mill limitation in whatever amount is necessary to pay debt service on those bonds. Section 5705.218, O.R.C., permits a school district to propose, as one ballot question, a bond issue and either an income tax for school district purposes (operating or permanent improvement) or a property tax levy for current operating expenses or permanent improvements or both.

##### 1.3.1 Election Procedures for Bond Issue.

The procedural steps to place a voted bond issue on the ballot are outlined in Section 133.18, O.R.C. For a school district, the steps are as follows:

.1 Resolution of necessity. The school district's board of education passes a resolution declaring the necessity of the bond issue.

.2 County auditor's certification. The county auditor estimates the average annual tax levy (stated in mills) required to pay debt service on the bond issue.

.3 Resolution to proceed. The board of education passes a resolution determining to proceed with the bond issue.

.4 Board of elections certification. The board of education certifies all of the foregoing documents to the board of elections of the school district's dominant county no later than ninety (90) days before the election.

Section 133.18(B), O.R.C., requires that the foregoing documents contain certain information, such as a well-defined purpose clause, stating the necessity of levying a tax outside the ten mill limitation to pay debt service on the bonds, the proposed election date, an estimate of the net average interest rate the bonds will bear, and the maximum maturity of the bonds.<sup>1</sup> There is no limit on the number of bond issues that may be submitted to the voters at any given election.

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<sup>1</sup>The maximum maturity of the bonds is calculated in accordance with Section 133.20, O.R.C., which assigns useful lives to certain categories of permanent improvements. If more than one category of improvement is involved in a single bond issue, a weighted average is made to calculate the maximum maturity of the bond issue. The term of the bonds may not exceed the maximum maturity calculated under Section 133.20, O.R.C.

### 1.3.2 Election Procedures for Bond Issue with Levy, Levies or Combined Levy.

The procedural steps for a combined bond/property tax question are in Section 5705.218, O.R.C. and are similar to those outlined in 1.3.1, except that a two-thirds vote is required for the resolutions and an apportionment is required if pursuing a combined operating and permanent improvement levy. A maintenance levy for a Commission project may also be combined with the questions in Section 5705.218, O.R.C. The levy portion may be for a fixed period of years or a continuing period of time. A combined bond/property tax question may only be submitted to the voters three times during any calendar year, (Section 5705.214, O.R.C.) and is not available to a joint vocational school district.

### 1.3.3 Election Procedures for Bond Issue Combined with Income Tax.

The procedural steps for a combined bond/income tax question are in Section 5748.08, O.R.C. and are similar to those outlined in 1.3.1, except that a two-thirds vote is required for the resolutions and the resolution of necessity must be certified to the County Auditor and the State Tax Commissioner no later than one hundred five (105) days before the election. The income tax may be on either Ohio adjusted gross income or only on earned income included in Ohio adjusted gross income, may be either for a fixed period of years or a continuing period of time and an apportionment is required if pursuing a combined operating and permanent improvement income tax. A combined bond/income tax question may only be submitted to the voters twice during any calendar year and, if submitted twice, one of the submissions must be at the November election. A combined bond/income tax question is not available to a joint vocational school district.

### 1.3.4 Borrowing Authority for Voted Debt.

Once a majority of the voters have approved the bond issue, and the contest period has run, the board of education may issue the bonds or notes in anticipation of bonds pursuant to Section 133.18(H), O.R.C., or Sections 5705.218 or 5748.08, O.R.C. The board of education may also issue notes in anticipation of levy or income tax proceeds, as outlined in 1.2.2 for permanent improvement levies and as outlined in Section 5748.05, O.R.C., for income taxes.

### 1.3.5 Debt Limitations Applicable to Voted Debt.

The securities issued pursuant to this type of financing are subject to the nine percent (9%) direct debt limitation, but are not subject to the ten mill limitation.

### 1.3.6 State Consent Required.

Under Section 133.06(C), O.R.C., if the amount of debt will exceed four percent (4%) of the tax valuation of the school district, the board of education must obtain the consent of the Superintendent of Public Instruction and the Tax Commissioner of Ohio in order to place the bond issue before the voters. The consent materials must be submitted no later than one hundred twenty (120) days before the election and must include the resolution authorizing the consent to be filed, a net indebtedness form, an incumbency certificate regarding school district officers, and the Ohio Department of Education's data form. This filing requirement is not necessary for

school districts participating in a Commission program and the bonds fund: a) the school district's local share of the basic project cost; b) state-required locally funded initiatives<sup>1</sup>; or c) site acquisition. A board of education also need not obtain consent if the bond issue it proposes to place before voters at the upcoming election is the identical question rejected at the election immediately preceding, and consent to place that question on the ballot had been previously obtained.

### 1.3.7 Practical Considerations Regarding Voted Debt.

.1 Purpose clause. The board of education should very carefully prepare its purpose clause in its bond election proceedings so that it complies with applicable laws, e.g. the "one purpose" rule,<sup>2</sup> yet is broad enough to encompass the project and permit the school district flexibility in the event other needs become apparent.

.2 Estimated average millage. The issue size, the estimated interest rate, the bonds' maximum maturity, and the current tax valuation<sup>3</sup> will be used to calculate the average annual levy that appears on the ballot. Accordingly, the issue size and estimated interest rate should be carefully selected. The maximum maturity of the bond issue should be carefully calculated. It may be most prudent to allocate bond proceeds to those categories of improvements having longer useful lives, if other components of the project can be financed out of other available revenues or out of investment earnings on the bond proceeds. In promoting the bond issue the county auditor's estimate of average annual levy should be recognized for what it is--only an estimate based on certain assumptions. Those assumptions may or may not be true at the time the securities are issued: interest rates may change significantly; the board of education may choose to have the principal of the bonds mature on a basis other than substantially equal annual installments (which the county auditor must use in making the millage calculation under Section 133.18(C), O.R.C.); the board of education may choose to issue securities for less than the maximum number of years for which they could have been issued; and the school district's tax valuation may have increased or declined significantly.

.3 Bonds or notes. The board of education must initially decide whether to issue long-term bonds or short-term bond anticipation notes. When long-term interest rates are very high, it may not be prudent to issue bonds but rather to issue notes and "renew" them from time to time until long term rates decline to more favorable levels. In addition, school districts often issue bond anticipation notes in order to raise cash quickly to pay imminent or preliminary expenses and to begin collection of property taxes, especially if the bonds are approved at the November election. Generally, in order to commence collection of property taxes for debt service: (1) bonds or notes must actually be issued; or (2) a firm plan must be in place to issue securities and the plan requires a

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<sup>1</sup> District-initiated locally funded initiatives would require the filing related to the entire bond issue amount.

<sup>2</sup>The "one purpose" rule is found in Section 133.18(A), O.R.C. For school districts, "one purpose" is defined in Section 133.01(Z), O.R.C., as any number of facilities and buildings for school district purposes, and related facilities.

<sup>3</sup>This figure may change during the course of a year.

debt service payment in the upcoming tax collection year. Voter approval of the bond issue, by itself, does not commence property tax collection. Also, issuing notes means taking the risk that interest rates may change dramatically during the term of the notes.

.4 Structure and sale. Along with decisions regarding the initial form of the debt (bonds vs. notes) come additional issues regarding structure and sale:

- negotiated sale versus a competitive bid sale;
- the process for selecting an underwriter for a negotiated sale;
- level debt service, which may approximate the ballot millage more closely, or level principal payments, which result in lower total interest cost;
- different interest rates for different maturities;
- desirability of including minibonds or capital appreciation bonds (CAB's) as an option;
- treating a portion of the gross proceeds of the sale of the securities or the proceeds of the securities as capitalized interest in order to defer full levy of the property taxes required for debt service or to make interest payments prior to the time of first collection;
- selling the securities at a discount;
- optional redemption of bonds at a premium;
- obtaining a rating or credit enhancement such as municipal bond insurance or participating in the Ohio School District Credit Enhancement Program under Section 3317.18, O.R.C.;
- issuing the bonds in "book entry only" form;
- whether to hire an outside bond registrar; and
- including issuance expenses in the pricing of the securities.

Other issues which may arise include the propriety of reimbursing the school district's general fund for moneys advanced before issuing securities for expenses associated with the project (see "Arbitrage and Rebate Under Federal Tax Law" herein) and, post issuance, the use of general fund moneys or investment earnings on bond proceeds for project costs or debt service.

## 1.4 Unvoted Debt.

### 1.4.1 Borrowing Authority for Unvoted Debt.

Sections 133.15 and 133.06, O.R.C., authorize a board of education to issue general obligation securities (bonds and bond anticipation notes) on an unvoted basis to finance "permanent improvements," *i.e.* improvements the school treasurer certifies as having a useful life of five (5) years or more.

### 1.4.2 Debt Limitations Applicable to Unvoted Debt.

The direct debt limitations, as well as the ten mill limitation, apply to this type of financing.

### 1.4.3 Practical Considerations Regarding Unvoted Debt.

The obvious advantage of this type of debt is that no vote of the people is required. However, unvoted debt does not produce a new source of revenue to pay debt service. Consequently, the school district board of education would have to pay debt service from currently available revenues appropriated for that purpose or use revenues from its share of the inside/unvoted millage. In addition, because of the strict one-tenth of one percent (1/10 of 1%) unvoted direct debt limitation, typically the amount of money available from this type of financing is too small to do a major construction or renovation project. This type of financing may be well-suited for minibonds, *i.e.*, bonds of a denomination of less than five thousand dollars (\$5,000).

## 1.5 Energy Conservation or "264" Notes.

House Bill 264 was the original legislation authorizing school districts to borrow money under special circumstances to finance qualified energy conservation improvements. This legislation has been amended several times since originally enacted.

### 1.5.1 Borrowing Authority for Energy Conservation Projects.

Sections 133.06(G), 3313.372, and 3313.373, O.R.C., enacted by H.B. 264, permit boards of education to undertake qualified energy conservation measures using three separate financing mechanisms, Section 3313.373, O.R.C. having a maximum term of ten (10) years and Sections 133.06(G) and 3313.372, O.R.C. each having a maximum term of fifteen (15) years.

.1 Section 133.06(G), O.R.C. --The board of education may issue unvoted general obligation securities in accordance with the Uniform Public Securities Law.

.2 Section 3313.372, O.R.C. --The board of education may issue unvoted notes which must be sold to the vendor. The notes may be secured by property taxes.

.3 Section 3313.373, O.R.C. --The board of education may enter into a "shared-savings contract" with the vendor. No securities are issued.

### 1.5.2 Debt Limitations Applicable to Energy Conservation Project Financings.

Under the unvoted direct debt limitation, securities issued pursuant to Section 133.06, O.R.C., may be issued in an amount up to nine-tenths of one percent (9/10 of 1%) of the school district's tax valuation. Securities issued under Section 133.06(G), O.R.C., are also subject to the nine percent (9%) direct debt limitation as well as the ten mill ("indirect") debt limitation. Securities issued under Section 3313.372, O.R.C., are subject to the ten mill limitation and are subject to a direct debt limitation of one percent (1%) of the school district's tax valuation if the notes are secured by property tax revenues. If, however, debt service on the notes will be paid from the savings realized by the conservation measures, notes issued for purposes of paying the school district's local share of basic project cost under a Commission program pursuant to Section 3318.052, O.R.C., are exempt from the direct debt limitation and may exceed one percent (1%) of the school district's tax valuation.

### 1.5.3 State Approval.

Both Sections 133.06(G) and 3313.372, O.R.C., require approval of the Commission prior to issuance of any securities. One of the elements of Commission approval is a finding that the amount spent on the energy conservation measures is not likely to exceed the amount of money the school district would save in energy costs and resultant operational and maintenance costs.

### 1.5.4 Practical Considerations Regarding Energy Conservation Project Financings.

Each of the financing mechanisms contains a specific exemption from competitively bidding the energy conservation project, although Sections 133.06(G) and 3313.372, O.R.C. require a two-thirds vote of the board of education in that regard. Because of the requirement of selling the notes to the vendor, Section 3313.372, O.R.C., notes may bear an interest rate higher than the market rate for tax exempt notes, unless the vendor agrees to assign the notes immediately to a bank or an investment banking firm. Finally, the shared-savings contract option of Section 3313.373, O.R.C., may be impractical due to the vendor's unwillingness to agree to be paid only from savings the project generates.

## 1.6 Land and Facilities Lease Arrangements.

### 1.6.1 Statutory Authority for Land Lease Arrangements.

Section 3313.37, O.R.C., authorizes a board of education, including a board of education of a joint vocational school district, (and a governing board of an educational service center), to acquire land by installment payments (with or without a mortgage), lease-purchase agreements, or by lease with an option to purchase. However, if the purchase price is to be paid over time, the payments cannot extend beyond five (5) years. The school district may, but is not required to, obtain voter approval for a special tax levy, in accordance with Section 5705.21, O.R.C., to provide a special fund to meet the future time payments.

### 1.6.2 Statutory Authority for Facility Lease-Purchase Arrangements.

Section 3313.375, O.R.C., authorizes a board of education, including a board of education of a joint vocational school district, (and a governing board of an educational service center or governing authority of a community school), to enter into a lease-purchase agreement which provides for the construction, lease, and eventual acquisition of a building or improvements to a building for any "school district purpose."<sup>1</sup> In addition, a school district may use a lease-purchase arrangement to finance the cost of making improvements to existing buildings and the furnishing and equipping of school buildings and facilities generally.

### 1.6.3 Facility Lease Provisions.

Facility leases must be structured as a series of one-year renewable lease terms over a maximum period of thirty (30) years, and the lease-purchase agreement must provide that the school district will acquire title to the building, in addition to the land on which the building is constructed, at the end of the lease term. The lease-purchase agreement may additionally require the school district to make a lump sum payment at the end of the lease term in order to acquire the building and land (more akin to a true lease with an option to purchase the building at fair market value at the end of the lease term). In conjunction with the lease-purchase agreement, the school district may grant leases, easements, and licenses for underlying land or facilities under the school district's control for terms not exceeding five (5) years beyond the final renewal term of the lease-purchase agreement.

### 1.6.4 Facility Lease Termination.

The lease-purchase agreement must permit the school district to terminate the lease at the end of any one-year term without penalty or additional cost.

### 1.6.5 Certificates of Participation.

In order to generate funds necessary to pay for the costs of construction or improvement of the building, the lease-purchase transaction often involves the use of certificates of participation ("COPs"), which grants the holder of the COP a security interest in the lease payments made by the school district. COPs are similar to bonds and notes but do not represent indebtedness of the school district for state law purposes. The proceeds of the sale of the COPs are used to pay construction costs in the same manner as bonds and notes are used to finance permanent improvement projects.

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<sup>1</sup> Although Section 3313.374, O.R.C., was enacted at roughly the same time to permit the lease-purchase of administrative office facilities, because office facilities are subsumed within the definition of "building for any school district purpose" under Section 3313.375, O.R.C., and because the requirements under Section 3313.374, O.R.C., are more cumbersome than those contained in Section 3313.375, O.R.C. any lease-purchase of office facilities should be undertaken pursuant to Section 3313.375, O.R.C.

### 1.6.6 Debt Limitations.

Section 3313.375, O.R.C., specifically provides that a school district's obligations under a lease-purchase agreement entered into under that section are exempt from the direct debt limitations.

### 1.6.7 Practical Considerations Regarding Facility Lease-Purchase Agreements.

Because a lease-purchase agreement does not involve the levy of an additional tax, a school district entering into such an arrangement must be able to identify a source of funds with which to make lease payments. Therefore, unless a school district is carrying a general fund surplus or is able to identify other moneys to devote to the lease payments (such as a permanent improvement levy), a lease-purchase arrangement will not be a feasible alternative, except for a small building addition.

## 1.7 Equipment Lease Arrangements.

### 1.7.1 Statutory Authority for Lease Arrangements.

Section 3313.37(B)(4), O.R.C., authorizes a board of education to acquire office equipment<sup>1</sup> and computer hardware and software<sup>2</sup> for instructional purposes by purchase, lease, installment payments, lease-purchase, or lease with an option to purchase. Payments cannot extend beyond five (5) years.

### 1.7.2 Debt Limitations.

If the financing lease is subject to annual appropriation, it is not debt for state law purposes and, accordingly, is exempt from the two "direct debt" limitations and exempt from the "indirect" or ten-mill limitation.

In "appropriation out" leases, the language in the lease should clearly state that the lease will terminate without further action or any penalty if funds are not appropriated.

### 1.7.3 Practical Considerations Regarding Lease Arrangements.

Many of the leasing companies that lease office equipment and computer hardware and software are national in scope, unfamiliar with Ohio legal requirements and reluctant to authorize modifications to their standard documents. Their standard documents will include an essential use certificate, as a hedge against nonappropriation, and an acceptance certificate identifying the equipment which should be carefully examined. The companies will typically take responsibility for filing any UCC financing statements and Form 8038-G to preserve the tax exemption. An

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<sup>1</sup> "Office equipment" is defined in the statute as including but not limited to typewriters, copying and duplicating equipment, and computer and data processing equipment.

<sup>2</sup> "Software for instructional purposes" is defined in the statute as including computer programs usable for computer assisted instruction, computer managed instruction, drill and practice, and problem simulations.

escrow may be required if the lessor is advancing a significant sum for equipment or technology acquisition that is going to be phased in.

## 1.8 Financing Lease Provisions Requiring Modification.

It is common for financing lease documents to have provisions that require modification to comply with Ohio law.

### 1.8.1 Disclosure in Secondary Market Transactions.

Section 9.94, O.R.C., prohibits third parties from selling fractionalized interests in any public obligations, including leases, without the knowledge and express written approval or authorization of each public issuer and, further, requires a provision to that effect in each lease or other public obligation.

### 1.8.2 Nonsubstitution.

Most nonsubstitution clauses are too onerous to comply with Section 3313.47, O.R.C., which vests management and control of schools in the board of education. Making such clauses subject to applicable state law or applicable public policy is insufficient to fix the problem, as are severability clauses.

### 1.8.3 Indemnification.

School districts have no express or implied authority to grant indemnification. OAG 2005-007 advises that Ohio counties may only provide indemnification to the extent the potential liability is quantified, appropriated and certified as available in accordance with Section 5705.41(D)(1), O.R.C. In addition, the indemnification clause may only obligate the county for the duration of the fiscal year in which the contract is executed. The analysis of OAG 2005-007 would also apply to school districts. It is uncertain whether this limit on indemnification can be addressed by making such a provision subject to applicable state law or applicable public policy.

### 1.8.4 Personal Property Taxes.

Ohio law provides that ultimate use controls whether liability for personal property taxes attach. A public use would not be subject to tax, even if title to the property used is held by another entity. Nevertheless, it is common for financing lease documents, particularly in the context of an equipment lease arrangement, to have a provision that any such taxes, if tax, pass through to the school district. Such a provision should be modified to acknowledge that the school district is a public entity exempt from personal property taxation, and, if possible, to provide that the school district will have no obligation to reimburse, by separate payment, the lessor for personal property tax paid by lessor and arising from the school district's use of the equipment in Ohio.

### 1.8.5 Certificate of Availability of Funds.

With respect to equipment lease arrangements, Section 3313.37(B)(4)(b), O.R.C., provides that if the purchase price is to be paid over a period of time, the contract must be considered a continuing contract under Section 5705.41, O.R.C.

### 1.9 Ohio School Facilities Commission.

#### 1.9.1 Classroom Facilities Assistance Program (CFAP).

The two steps to participate in CFAP are Commission conditional approval and Controlling Board approval (Sections 3318.03 and 3318.04, O.R.C.).

.1 Conditional approval. The Commission is required to periodically assess classroom facility needs in the state to identify school districts needing additional or renovated classroom facilities<sup>1</sup> and the cost<sup>2</sup> thereof. This periodic assessment is confirmed by on-site visits<sup>3</sup> in ascending, wealth-ranked (by a three-year average of adjusted valuation per pupil, further adjusted for those districts experiencing an "open enrollment net gain" under Section 3318.011, O.R.C.) percentile order<sup>4</sup> that also: (1) evaluate the need for renovations and additions versus an acquisition or new construction and the practicability of meeting such needs; (2) at the school district's request, examine any classroom facilities needs assessment and corresponding master plan the school district has developed; (3) determine the amount of the cost of such facilities the school district is able to pay; and (4) determine the remaining amount of such cost that shall be paid by the State. Other determinations must also be made by the Commission relating to the following: sound educational practice; student and staff safety; orderly school district reorganization and consolidation; projected enrollment of three hundred fifty (350) pupils in each classroom facility

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<sup>1</sup> "Classroom facilities" includes space necessary for operating a vocational program for secondary students in any school district operating such a program.

<sup>2</sup> Cost under CFAP is "basic project cost", a defined term under Section 3318.01(L), O.R.C. The calculation of basic project cost must take the following into consideration: (1) square footage and cost per square foot; (2) variation across the state in construction and related costs; (3) the cost of the installation of site utilities and site preparation; (4) the cost of demolition of all or any part of any existing classroom facilities that are abandoned under the project; (5) the cost of insuring the project until completion; (6) the contingency reserve amount prescribed by the Commission under Section 3318.086, O.R.C.; and (7) professional planning, administration and design fees.

<sup>3</sup> The Commission may limit the on-site visits based on the moneys available and necessary to undertake projects that year.

<sup>4</sup> The Commission is directed to identify the next ten school districts, from the lowest to the highest in order of the ranking calculated pursuant to the previous fiscal year under Section 3318.011, O.R.C., that have not already been conditionally approved for CFAP assistance. The identification of the ten school districts' must occur each fiscal year at the same time the Commission conditionally approves projects for CFAP. The ten ranked school districts will have priority over all other schools districts except for: additional assistance (Section 3318.04(B)(2), O.R.C.); exceptional needs (Section 3318.37, O.R.C.); accelerated urban (Section 3318.38, O.R.C.); and school districts previously conditionally approved by the Commission and the state controlling board, but unable to fund the local share and maintenance obligation within a year of such approvals (Section 3318.05, O.R.C.).

included in a project; whether there is good cause for renovation versus new construction such as historical value; and whether the project relates to classroom facilities financed under CFAP in the last twenty (20) years and the school district qualifies for additional assistance. Such confirmations and affirmative determinations constitute "conditional approval".

Any school district not yet eligible under CFAP may request the Commission to assess its classroom facilities needs. Such assessment must be done within two (2) years following such request.

- a. Additional assistance. Additional assistance is available for the following:
  - 1) enrollment - an exceptional increase in enrollment significantly above the design capacity of the prior project; or
  - 2) limited double back - before May 20, 1997 - five (5) school districts per fiscal year, if the percentile in which the school is located is eligible and the school district extends its maintenance obligation, either by vote of the people for a voted one-half (0.5) mill levy or by pledging property or income taxes or a combination thereof. The Commission must establish application procedures, deadlines and priorities, and may waive design specifications if the current project renovates a previous project. The Commission may deny additional assistance if the Commission determines the school district's existing classroom facilities are adequate to meet its needs.
  - 3) assessment oversights and deficiencies - after May 20, 1997 - the project still must be under construction and additional assistance is for correcting those conditions. The school district must pay the local share of the cost or, if undue hardship, enter into a loan agreement with the state for a ten (10) year maximum term.<sup>1</sup>

.2 Controlling Board approval. Once conditional approval is received, the Commission then submits the proposal to the Controlling Board for approval of the Commission's determinations and the state share of the basic project cost.<sup>2</sup>

### 1.9.2 School District Financial Participation in CFAP.

School district financial participation in CFAP varies with school district wealth. School districts still have to fund maintenance of the project and provide funds for the local share of the basic project cost. However, the school district only has to provide funds equal to the greater of

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<sup>1</sup> Loans under this section are exempt from the direct debt limitations.

<sup>2</sup> The state now encumbers only those state funds needed for the state share for the current fiscal biennium.

either of the following (and not greater than ninety-five percent (95%) of the total basic project cost):

- a. an amount that increases the total net indebtedness, as of the date the controlling board approved the project, to within five thousand dollars (\$5,000) of the required level of indebtedness under CFAP<sup>1</sup>; or
- b. an amount equal to the required percentage of project costs under CFAP.

.1 Required level of indebtedness. Section 3318.01(J), O.R.C., defines required level of indebtedness as follows:

- a. first percentile, five percent (5%) of the tax valuation<sup>2</sup> of the school district;
- b. subsequent percentiles, five percent (5%) of the tax valuation of the school district plus two one-hundredths of one per cent (0.02%) multiplied by the percentile in which the district ranks minus one (1).

The percentile rankings are determined by the Ohio Department of Education (the "Department") which ranks school districts according to a three-year average adjusted valuation per pupil for the current and two (2) preceding fiscal years. The formula for such calculations is outlined in Section 3318.011, O.R.C. The school districts are ranked from the lowest to highest adjusted valuation per pupil and then divided into percentiles.

.2 Required percentage of basic project costs. Section 3318.01(K), O.R.C., defines required percentage of basic project costs as one percent (1%) of the basic project costs times the percentile in which the district ranks as of the time the controlling board approved the project.

.3 Segmenting Option (non-Accelerated Urban). Section 3318.03(A)(2)(b) provides that for segments to be completed separately, an amount necessary to raise the school district's net bonded indebtedness, as of the date of state controlling board project approval, to within five thousand dollars (\$5,000) of the following:

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<sup>1</sup> In calculating net indebtedness, amounts in the school district's bond retirement fund are to be included as well as any amounts the school district is obligated to pay under lease-purchase agreements entered into under Section 3313.375, O.R.C. Site-related debt is not included, nor is the par value of bonds authorized by the voters and the proceeds of which will be used to provide any part of the school district's portion of the basic project cost.

<sup>2</sup> Tax valuation under this definition is for the year preceding the year in which the controlling board approved the project under Section 3318.04, O.R.C.

$$\frac{\text{Required level of indebtedness} \times \text{basic project cost of controlling board-approved segment}}{\text{basic project cost of entire classroom facilities' needs}} \\ \text{(determined jointly by Commission and school district)}$$

Further, the school district portion of a segment must be in a minimum amount of: 0.04 x the school district's valuation at the time the agreement for the segment is executed, unless the segment is for the remainder of a school district's entire classroom facilities needs. Plus, the maintenance obligation runs for twenty-three (23) years from the date the first segment is undertaken.

### 1.9.3 CFAP Election Proceedings.

Section 3318.05, O.R.C, provides that the conditional approval of the Commission shall lapse and the state controlling board's encumbered funds for the project shall be released unless, generally, within one hundred twenty (120) days of certification of the conditional approval, the school district's board of education accepts the approval and, within one (1) year of the date of such certification, the school district provides funds for the local share and for maintenance of the project necessary for participation in CFAP.<sup>1</sup> If the board of education or the electors fail to take the foregoing steps, and the amount reserved and encumbered for the school district's project is released, the school district is given first priority for project funding as such funds become available.

All of the following may be included as one ballot question under Section 3318.056, O.R.C.:

1. bond issue to fund local share;
2. bond issue or permanent improvement levy to fund CFAP sites;
3. maintenance levy (one-half (0.5) mill, twenty-three (23) years);
4. bond issue for locally funded initiatives (non-CFAP) (Section 133.18, O.R.C.);
5. operating<sup>2</sup> or permanent improvement levy (Section 5705.21, O.R.C.);
6. combined bond issue and tax levy (levy portion may be operating,<sup>22</sup> permanent improvement or both) (Section 5705.218, O.R.C.); or
7. income tax (Section 5748.08, O.R.C.).

- .1 Alternatives to fund the local share.<sup>3</sup>

<sup>1</sup> If any related ballot question(s) are not approved within one year, the local share will be recalculated in accordance with subsequent controlling board approval.

<sup>2</sup> Operating revenue generated by such a question must be specifically for the school district's Commission facilities.

<sup>3</sup> The local share may be recalculated in certain circumstances regarding gas pipelines if there is a reassessment of property owned by natural gas companies.

- a. Bonds. A bond issue must be in the alternative amounts discussed previously and the maximum maturity of the bonds is calculated pursuant to Section 133.20, O.R.C. (the standard formula of the Uniform Public Securities Act). The bond issue may be an incremental bond issue of more than one (1) series, not to exceed five (5).<sup>1</sup>
- 1) State consent. Under Section 133.06(C) O.R.C., if the amount of debt will exceed four percent (4%) of the tax valuation of the school district, the board of education must obtain the consent of the Superintendent of Public Instruction and the Tax Commissioner of Ohio in order to place the bond issue before the voters. The consent materials must be submitted no later than one hundred twenty (120) days before the election and must include the resolution authorizing the consent to be filed, a net indebtedness form, an incumbency certificate regarding school district officers, and the Ohio Department of Education's data form. This filing requirement does not apply to bond issues that fund: a) the school district's local share of the basic project cost; b) the state-required locally funded initiatives;<sup>2</sup> or c) site acquisition. A board of education also need not obtain consent if the bond issue it proposes to place before voters at the upcoming election is the identical question rejected at the election immediately preceding, and consent to place that question on the ballot had been previously obtained.
- b. Funds from or bonds leveraged by permanent improvement levy, income tax or combination thereof. A continuing permanent improvement levy or income tax or combination thereof may be used to provide funds or to issue either general obligation or special obligation securities under the Uniform Public Securities Act to pay all or part of the local share.
- c. Local donated contribution. A school district may apply a local donated contribution toward the local share. Under Section 3318.084, O.R.C., local donated contribution means any of the following:
- 1) moneys irrevocably donated or granted to a school district by a source other than the state which the board has authority to apply to the project and does so by resolution; or

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<sup>1</sup> The incremental bond resolutions may state the number of series, the principal amount of each series, the approximate date each series will be issued, and may provide that no series, or any portion thereof, may be issued before those dates. The ballot form is provided in Section 3318.062, O.R.C.

<sup>2</sup> District-initiated locally funded initiatives would require the filing related to the entire bond issue amount.

- 2) any irrevocable letter of credit issued on behalf of a school district or cash a school district has on hand, if encumbered by the school district for the local share and approved by the Commission in consultation with the Department.
- 3) Any money spent by a source other than the school district or the state for construction or renovation of specific classroom facilities that have been approved by the Commission as part of the basic project cost.<sup>1</sup>

The local donated contribution must first be deposited in the project construction fund (or an agreement executed) before any state moneys are released.

.2 Alternatives to fund the maintenance obligation.

- a. Tax levy.<sup>2</sup> The levy for maintenance of the project is a tax outside the ten-mill limitation, subject to the reduction factor under Section 319.301, O.R.C. (HB 920). The levy must be at the rate of one-half (0.5) mill for each dollar of valuation for twenty-three (23) years, unless the amount to be collected in the first twelve (12) months is less than ten percent (10%) of the amount of money that the school district was required to deposit into its capital and maintenance fund during the most recent fiscal year. Proceeds of the levy are to be used in accordance with a Commission-approved maintenance plan.
- b. Earmarking permanent improvement levy, income tax or combination thereof.<sup>27</sup> A continuing permanent improvement levy, under either Section 5705.21 or 5705.218, O.R.C., or income tax or combination thereof may be used to generate all or part of the funds necessary to meet the maintenance obligation, if the proceeds may lawfully be used therefor.
- c. Local donated contribution as offset to maintenance contribution. A school district may apply a local donated contribution toward the maintenance obligation to offset all or part of such maintenance obligation.<sup>3</sup> For a partial offset, a rate of tax less than one-half (0.5) mill

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<sup>1</sup> The Commission, the school district and the entity providing the local donated contribution must enter into an agreement identifying the classroom facilities to be acquired and the agreement must include stipulations that require an audit by the Commission of the expenditure of the local donated contribution and that specify the maximum amount of the credit to be allowed for these expenditures. State moneys may be released, even if the entity providing the local donated contribution has not spent the moneys, as long as the agreement has been executed.

<sup>2</sup> If appropriately indicated on the ballot, funds generated from a voted tax levy (either under Section 3318.05(B) or (C), O.R.C.) may be used for infrastructure improvements.

<sup>3</sup> A schedule for depositing such moneys is required and, for a complete offset, must demonstrate full funding of the maintenance obligation by the anticipated completion date of the project.

will be calculated. Any offset will be tested at the end of the twenty-three (23) year period against the amount that would have been generated by a one-half (0.5) mill levy. If the school district is short of that amount, the school district pays the difference. If the school district is over that amount, no payments are made by the school district or the Commission.

- d. Annual transfer (inside millage, etc.). Upon Commission approval, a school district may annually transfer each year for twenty-three (23) years that portion of the funds necessary to meet the maintenance obligation. A school district may rescind such decision only if a property tax levy has been approved by its voters under Section 3318.063, O.R.C.: (1) for the remainder of the twenty-three (23) year period, (2) at a rate not less than one-half (0.5) mill for each dollar of valuation; and (3) such levy continues to be collected as approved by the electors (not reduced by voter-initiated petition). School Districts using this alternative are not: (1) relieved from their obligation to maintain their capital and maintenance set-aside under Section 3315.18, O.R.C.; or (2) eligible for maintenance levy equalization.

The local donated contribution must first be deposited (or an agreement executed) in the capital and maintenance fund before any state moneys are released.

#### 1.9.4 Commission Prerequisites for CFAP State Share.

.1 State Agreement. Prior to entering into the state agreement, the school district's board of education must pass a resolution authorizing the board's president and treasurer to sign the agreement on behalf of the school district. The form of agreement (prepared by the Commission) provides for the following:

- levy of any tax required for maintenance and, if applicable, for the issuance of bonds or notes to pay the school district's local share;
- ownership of or interest in the project during the construction shall be divided between the state and the school district, according to their respective contributions to the cost of the project; provided, however, that title to any real property purchased with moneys in the construction account shall be held in the name of the state;
- when obligations issued by the state for the project are no longer outstanding, the state's portion of title to the project is transferred to the school district;
- the establishment of a construction fund for payment of costs of the project with all payments from such fund to be made using vouchers that require approval from both the school district and the Commission;

- school district maintenance of the project until obligations issued by the state therefor are no longer outstanding, and such maintenance to be in accordance with a Commission-approved plan;
- state funds reserved to pay the state share be spent first, unless the local share must be expended for federal tax reasons or the school district is in the Commission's Accelerated Urban Initiative Program; and
- a provision stipulating that the Commission may prohibit a school district from proceeding with any project if the Commission determines that the site is not suitable for construction purposes.
- a provision stipulating that for continued release of project funds, a school district shall comply with Section 3313.41, O.R.C. regarding disposal of facilities for sale, prior to demolition at a non-replacement site, including notification to the Ohio Department of Education and the Ohio community school association;
- eligibility for the one-half (0.5) mill maintenance levy equalization fund.

.2 State Plans and Specifications. Plans and materials proposed for use in the project must comply with specifications for plans and materials established by the Commission.

.3 Investment Earnings. Section 3318.12, O.R.C., requires that all investment earnings, on both the local share and state share, be initially credited to the construction fund pro rata to the local share and state share, respectively, via a special cost center for each.

Pending Commission project completion, if there is no current budget overrun or new LFI due to a budget overrun, the school district may divert investment earnings on its local share to LFIs related to the Commission project, and not just Required LFIs.<sup>1</sup> If a school district chooses to use investment earnings thusly, and project costs later increase such that there is a shortfall, the school district must replenish the local share to the full extent the investment earnings were diverted, as well as fund the local share of the budget increase.

After Commission project completion, if investment earnings remain that are attributable to the local share, such investment earnings may be:

- Retained in Fund 010 for future projects;
- Transferred to Fund 034 (Commission Project Maintenance); or
- Transferred to Fund 003 (School District Permanent Improvement).

<sup>1</sup> "Required LFIs" are those required by Commission "to pay the cost of classroom facilities or portions or components of classroom facilities that are not included in the district's basic project cost but that are related to the district's project." A school district must do them to continue to qualify for the State Share, but Commission does not co-fund Required LFIs.

### 1.9.5 Exceptional Needs School Facilities Assistance Program (ENP).

.1 Eligibility. Under Section 3318.37, O.R.C., a school district must be "low wealth" (first through seventy-fifth percentiles as determined by the Department) or have a large land area with an exceptional need for new facilities in order to protect the health and safety of all or a portion of its students.<sup>1</sup> Assistance under this program does not bar participation in CFAP for the remainder of the school district's classroom facilities needs.<sup>2</sup>

.2 Participation Procedure. A school district shall apply to participate, and the Commission shall evaluate and prioritize such applications, pursuant to Commission guidelines. The Commission may conduct on-site evaluations as part of the evaluation process. The school district's local share of the basic project cost shall be the required percentage of project cost and the local share and maintenance obligation may be funded in any manner provided by Chapter 3318, O.R.C.

### 1.9.6 Extreme Environmental Contamination of School Facilities Program.

A school district, regardless of whether it meets the eligibility requirements of the Exceptional Needs School Facilities Assistance Program, may, if it qualifies under the Extreme Environmental Contamination of School Facilities Program, relocate or replace school facilities, as a result of extreme environmental contamination. The Commission will determine whether the contamination has made the school facilities no longer suitable for use as school facilities. The school district's contribution to replace the contaminated facility is limited to fifty percent (50%) of the total project cost, and the school district may use restitution funds to reduce its contribution to the project costs. The Commission, also, may determine that it can fund a district-wide project, if the other school facilities not affected by the contamination ultimately will need replacement.

### 1.9.7 Expedited Local Partnership Program (ELPP).

.1 Eligibility. Under Section 3318.36, O.R.C., the Commission may enter into agreements with school districts for ELPP. Under such an agreement, a school district may use "local resources"<sup>3</sup> to proceed with new construction or major repairs of a discrete part of the school district's total classroom facilities needs, prior to CFAP eligibility, and may apply qualifying expenditures toward its local share when the school district becomes eligible for CFAP.<sup>4</sup>

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<sup>1</sup> No school district reasonably expected to receive assistance under CFAP within three (3) fiscal years after the year of application is eligible to participate, as well as school districts participating in ELPP, with certain limited exceptions. "Large land area" means a territory of greater than three hundred (300) square miles.

<sup>2</sup> An Exceptional Needs Program facility will not be included when the remainder is done unless enrollment has increased per Section 3318.04, O.R.C.

<sup>3</sup> "Local Resources" means any moneys generated in any manner permitted for a school district to raise the local share of a project undertaken pursuant to ELPP.

<sup>4</sup> Any school district reasonably expected to receive assistance under CFAP within two (2) fiscal years is not eligible to participate in ELPP.

.2 Participation Procedure. The school district must pass a resolution indicating how it will fund the discrete part of its classroom facilities needs and forward such resolution to the Commission. The school district may proceed with a discrete portion of its project as soon as the Commission and the Controlling Board have approved the basic project cost of the district's classroom facilities needs (local and state share percentages).<sup>1</sup> Similar to CFAP, a school district has a year from such approval to provide funding, or the master plan and share percentages lapse. The maintenance obligation may be funded as follows:

- a. maintenance levy (either separate ballot question or combined with the questions under Section 5705.218, O.R.C.);
- b. earmarking the proceeds of a continuing permanent improvement levy (no reference to a two mill threshold) or continuing income tax;
- c. a local donated contribution; or
- d. upon Commission approval, an annual transfer.

A school district may opt to delay the foregoing until the school district becomes eligible for the state share under CFAP. No state share moneys under CFAP will be released until the maintenance obligation is funded. If a school district determines to pursue the maintenance levy and not opt to delay, the maintenance levy can be combined in a single ballot with the questions presented under Section 5705.218, O.R.C.

The best practice may be opting to delay, but pursuing a bond issue combined with a continuing permanent improvement levy under Section 5705.218, O.R.C., and sizing the permanent improvement levy appropriately to satisfy the maintenance obligation, required when the school district ultimately qualifies for CFAP, and any non-OSFC needs (Section 3318.052, O.R.C.).

.3 Recalculations and Reassessments. If a school district becomes eligible for CFAP based on its percentile ranking, the Commission shall conduct a new assessment of the school district's classroom facilities needs and recalculate the basic project cost. The school district's percentage of the recalculated cost will be the same as with the original cost. If an ELPP district has not begun its ELPP project at the time it becomes eligible for CFAP, all ELPP assessment and agreement documents become void.

- a. Reimbursement. If recalculation causes the school district's local share to dip below school district resources applied, within one (1) year after recalculation the Commission may grant the school district the difference, up to the recalculated state share. Such reimbursement is only for local

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<sup>1</sup> Commission must use an adjusted valuation formula instead of three year average for districts with ten percent (10%) or greater decreases in valuation due to decreases in the assessment rate of taxable property of an electric company.

resources that the school district has applied toward construction costs for classroom facilities approved by the Commission, not associated financing costs. However, such reimbursement: (1) may, at the option of the school district, first be used to replace local resources from its general or permanent improvement funds to the extent that those local resources fronted the state share; (2) if not used as replacement funds, must be used for debt service for the school district's project, including placing such reimbursement in an escrow fund under Section 133.34(D), O.R.C.

#### 1.9.8 Emergency Projects.

Under Section 3318.351, O.R.C., the Commission will distribute grants to eligible school districts for emergency projects. "Eligible school districts" are those in the first through one-hundredth percentiles as determined by the Department. An "emergency project" is a reconstruction, renovation or repair of classroom facilities because of damage due to an act of God, not age of the facilities or by lack of timely maintenance. Grants may only be used for costs not covered by insurance or public or private emergency assistance.

#### 1.9.9 Vocational Facilities Assistance Program.

Section 3318.40, O.R.C., establishes a vocational school facilities assistance program ("VFAP") under which the Commission is to assist joint vocational school districts in the acquisition of classroom facilities suitable for vocational education programs. VFAP is available exclusively for joint vocational school districts, is to be administered by the Commission and is structured similarly to CFAP. All references in the Ohio Revised Code to "vocational education" are deemed to refer to "career technical education" pursuant to Section 3303.01, O.R.C. As used in Sections 3318.40 to 3318.45, O.R.C., the terms "Ohio School Facilities Commission", "classroom facilities", "project" and "basic project cost"<sup>1</sup> have the same meanings as in Section 3318.01 O.R.C., (See 1.9.1.1 hereof).

1.9.9.1 Ineligible Programs/School Districts. Section 3318.40(C), O.R.C. sets forth certain programs which shall not be funded by the Commission, including exclusively adult education programs or commercial driver's education programs. In addition, the Commission shall not provide assistance to any school district to acquire classroom facilities for vocational educational instruction at facilities under the control of such school district, if that school district is a member of a joint vocational school district.

1.9.9.2 Commission Assessment and Approval. Beginning July 1, 2003, the Commission annually may set aside up to two percent (2%) of amounts appropriated to the Commission for VFAP programs.

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<sup>1</sup> For a joint vocational school district, the term basic project cost and the basic project cost calculation shall also take into account the types of laboratory spaces and program square footages needed for the vocational education programs for high school students offered by the joint vocational school district.

Section 3318.42, O.R.C., generally requires the Ohio Department of Education to perform a percentile ranking of each joint vocational school district based on each joint vocational school district's three year average valuations per pupil for the current and preceding two (2) fiscal years, with the joint vocational school district with the lowest three (3) year average receiving the highest priority for assistance. Further, after making such assessments, the Commission is directed to determine the applicability to joint vocational school districts of the design requirements in place with respect to other CFAP projects.

The Commission is required to annually assess the classroom facilities needs of the number of joint vocational school districts the Commission reasonably expects to be able to provide with assistance. Pursuant to such assessment, the Commission shall determine:

- the number of facilities to be included in a project, and the basic project cost of the project.
- the joint vocational school district's portion of the basic project cost, provided that no joint vocational school district's portion of the basic project cost shall be less than twenty-five percent (25%) or greater than ninety-five percent (95%) of the basic project cost.
- the remaining portion of the basic project cost that shall be supplied by the State.
- the amount of the State's portion of the basic project cost to be encumbered in the current and subsequent fiscal bienniums from the two percent (2%) set aside.

In many circumstances, the VFAP process for a joint vocational school district parallel the approval requirements for classroom facilities projects for non-joint vocational school districts as set forth in 1.9.1 through 1.9.4 hereof. For instance, divisions (A) and (C) of Section 3318.03, O.R.C., shall apply in assessing the needs of a joint vocational school district and shall be a part of the Commission's conditional approval process.<sup>1</sup> Further, no joint vocational school district that receives VFAP assistance of the Commission shall have another project conditionally approved for twenty (20) years, absent a showing of an exceptional change in circumstances.

1.9.9.3 Conditional Approval. If the Commission makes a determination based generally on the matters set forth in 1.9.10.2 in favor of the acquisition of classroom facilities by

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<sup>1</sup> Section 3318.03(A), O.R.C., requires the Commission to examine any classroom facilities needs assessment that has been conducted and any master plan developed for meeting the facility needs of the joint vocational school district. Section 3318.03(C), O.R.C. requires the Commission to make a determination that proposed project conforms to sound education practice, that such project is in keeping with an orderly process of school district reorganization and consolidation and that the proposed enrollment in the project is at least three hundred fifty (350) pupils.

a joint vocational school district for a vocational education project, such project shall be conditionally approved and:

- The Commission's conditional approval shall be submitted to Controlling Board for approval.
- In the event of Controlling Board approval, the Commission shall certify the approval to the board of education of the joint vocational school district.
- The Commission shall encumber the approved funds for the current fiscal year.

Such conditional approval shall lapse on essentially the same terms as a conditional approval for a non-joint vocational school districts, i.e. unless:

- The joint vocational school district Board of Education approves the Commission approval within one hundred twenty (120) days; and
- Within one (1) year the joint vocational school district electors vote favorably to fund the joint vocational school district's local share of the basic project cost, including maintenance of the project.

If the foregoing conditions are satisfied the Commission and the joint vocational school district shall enter an Agreement (See Section 1.9.4.1 hereof) for the project and shall proceed with development of plans, cost estimates, designs, drawings and specifications.

1.9.9.4 Financial Participation in VFAP. Similar to CFAP programs, a joint vocational school district may generate the local share of the basic project cost generally from any combination of sources set forth in Section 1.9.3, other than an income tax, i.e., the issuance of bonds, locally donated contributions, an operating or permanent improvement levy under Sections 5705.21 (five (5) years or continuing) or 3311.21 (ten (10) years), O.R.C. In addition, Section 3318.44, O.R.C., authorizes joint vocational school districts to issue unvoted bonds backed by a voted permanent improvement levy. Finally, under Section 3318.41, O.R.C., there is a simultaneous payout of the local and State shares in the construction fund in accordance with the respective percentages of project cost.

If a joint vocational district proposes to issue bonds to generate all or a portion of such school district's local share of the basic project cost, the board of education of such joint vocational school district must adopt a resolution of necessity by vote of two-thirds of its members, under Sections 3311.20 and 133.18, O.R.C. If a joint vocational school district deems it necessary to acquire a site for the proposed classroom facilities, the acquisition of such site may be accomplished by an issue of bonds or by a permanent improvement levy. A joint vocational school district may not combine a bond issue with a levy as one ballot question under Section 5705.218, O.R.C.

1.9.9.5 Vocational Maintenance Funding. A joint vocational school district must fund maintenance of the classroom facilities in order for the district to receive conditional approval of the Commission of a classroom facilities project for vocational education. Maintenance funding shall be annual for twenty-three (23) years and in the amount of one and one-half percent (1.5%) of the current insurance value of the Commission project, but does not have to be identified and funded up front.

1.9.10 Vocational Expedited Local Partnership Program. Under Section 3318.46, O.R.C., a joint vocational school district may enter into an agreement with the Commission under which the joint vocational school district may proceed with construction or major repairs of classroom facilities through the expenditures of local resources prior to the joint vocational school district's eligibility for State assistance. The program is similar to ELPP.

#### 1.10 Jointly Constructed and Controlled Improvements; Gifts.

Increasingly, boards of education try to leverage bond proceeds with revenue from outside sources for construction and operation of certain school district permanent improvements, such as fieldhouses, natatoriums and other recreation centers. Typically, title to the permanent improvement stays with the school district but the facility is available to the community during nonschool hours. Contributions may be in the form of cash, materials or services and may come from a variety of sources: community organizations, individuals or other political subdivisions.

.1 Authority for Participation. The most efficient way to accomplish the goal of joint construction and operation of a school district permanent improvement is to create it under one of the joint control methods permitted by Sections 755.14 and 755.16, O.R.C.:

- a. a joint recreation district;
- b. a joint venture between the school district and the political subdivision with control of the permanent improvement vested in a joint recreation board; or
- c. a joint venture agreement which would list the responsibilities of both the school district and the political subdivision without forming either a joint district or joint board.

.2 Practical Considerations Regarding Jointly Constructed and Controlled Improvements. Note that the above options all contemplate joint control by only political subdivisions or an educational service center; the participation of other parties, commonly a nonprofit entity such as a YMCA, would have to be through a lease or management contract. Also, although user fees are generally charged to offset operating expenses, participating political subdivisions may have to levy taxes or use moneys from their treasuries to cover operating deficiencies of the permanent improvement under Section 755.18, O.R.C. Accordingly, politically the school district may want to restrict use of the permanent improvement to school district residents. Finally, depending on the amount of and manner in which school district bond proceeds are spent on the joint permanent improvement, the tax exempt status of an entire bond issue might

be jeopardized prior to the maturity of the bonds if use arrangements are not carefully structured (see "Private Use Under Federal Tax Law" herein).

.3 Gifts. Under Section 3313.36, O.R.C., school district are permitted to accept gifts with conditions and honor the same, as long as control of the schools is not surrendered.

## 1.11 Federal Securities Law.

### 1.11.1 Primary Offering Disclosure.

.1 General Requirements. Securities and Exchange Commission Rule 15c2-12, requires underwriters participating in primary offerings of securities such as bonds and bond anticipation notes of \$1,000,000 or more to obtain, review, and distribute to investors copies of the issuer's official statement.

.2 Exemptions. The rule contains exemptions for underwriters participating in offerings of tax-exempt securities issued in minimum denominations of \$100,000 and that (a) are issued for not more than nine (9) month terms, or (b) are sold to no more than thirty-five (35) sophisticated investors who are buying for their own accounts.

### 1.11.2 Secondary Market (Continuing) Disclosure.

.1 General Requirements. Rule 15c2-12 imposes a duty on underwriters to provide secondary market information to potential purchasers. Underwriters subject to the rule are prohibited from purchasing or selling securities unless the underwriter reasonably determines that the issuer of the securities (i.e., the taxing authority) has undertaken to provide the following information in a timely manner:

- a. "annual financial information" for the issuer;
- b. if not submitted as part of the annual financial information, then when and if available, audited financial statements for the issuer; and
- c. notice of any of the following events with respect to the securities being offered, if material ("Material Events"):
  - (1) Principal and interest payment delinquencies;
  - (2) Non-payment related defaults;
  - (3) Unscheduled draws on debt service reserves reflecting financial difficulties;
  - (4) Unscheduled draws on credit enhancements reflecting financial difficulties;
  - (5) Substitution of credit or liquidity providers, or their failure to perform;
  - (6) Adverse tax opinions or events affecting the tax-exempt status of the security;

- (7) Modifications to rights of security holders;
  - (8) Bond calls;
  - (9) Defeasances;
  - (10) Release, substitution, or sale of property securing repayment of the securities; and
  - (11) Rating changes.
- d. notice of failure to provide required annual financial information on or before the date specified in the agreement.

The information listed above must be provided by the issuer of the securities to the Electronic Municipal Market Access ("EMMA") system of the MSRB (available at: [emma.msrb.org](http://emma.msrb.org)). Any information submitted by an issuer to EMMA must be by electronic submission in an electronic portable document format ("PDF") that contains a word-search function permitting a user to search the information.

- e. Issuers may not condition their obligation to provide notice of Material Events on their actually having knowledge of the Material Event.

.2 Requirements of Written Agreement or Contract. The undertaking to provide continuing disclosure is required to:

- a. Specify, in reasonable detail, the type of financial information and operating data to be provided;
- b. Specify, in reasonable detail, the accounting principles to be used in preparing the financial statements and whether they will be audited; and
- c. Specify the date on which the annual financial information will be provided and to whom it will be provided.

.3 Recommendation Prohibition. Brokers and dealers in municipal securities are prohibited from recommending an issue of securities for purchase or sale unless the broker has procedures in place to receive notice of Material Events and other information.

.4 Exemptions.

- a. Same as for primary offerings (as described in Section 1.5.1)
- b. At the time of issuance:
  - (1) the issuer has no more than \$10,000,000 of securities outstanding, including the proposed issue and excluding any exempted issues;
  - (2) the issuer undertakes, by written agreement, to provide to EMMA:
    - at least annually, financial information or operating data for the issuer including, at a minimum, that financial information and

operating data which is customarily prepared by the issuer and is publicly available;

- in a timely manner, notice of Material Events.

(3) the final official statement identifies by name, address, and telephone number the person from whom such information can be obtained.

- c. If the maturity of the proposed securities is less than eighteen (18) months, the issuer does not have to comply with the annual reporting requirements but will be subject to the official statement review and delivery requirements and to the Material Events reporting requirement.

## 1.12 Federal Tax Law.

### 1.12.1 Arbitrage and Rebate.

Section 103(a) of the Internal Revenue Code ("I.R.C.") exempts the interest earned on bonds and notes of governmental units from federal income taxation. Consequently, a school district can typically sell its bonds or notes at an interest rate significantly lower than the prevailing taxable interest rates. The lower interest rate allows the school district to realize an arbitrage opportunity by investing the note or bond proceeds in higher yielding taxable investments during the period between issuing such securities and paying construction expenses. Normally, the Internal Revenue Service penalizes these arbitrage earnings by restricting reinvestment of such proceeds and requiring rebate of arbitrage earnings, with certain exceptions.

.1 Arbitrage Temporary Period restrictions. Section 148(c), I.R.C., permits a school district to invest bond proceeds in investments with a higher yield than that of the bonds for a temporary period until the proceeds are needed for the project being financed. To qualify for the temporary period exception for capital projects, a school district must satisfy the following three-part test:

- a. Expenditure test. The school district must reasonably expect to expend eighty-five percent (85%) of the bond proceeds on project expenses within three (3) years of the date of issue (Treas. Reg. §1.148-2(e)(2)(i)(A)).
- b. Time test. The school district must incur, within six (6) months of the date of the issue, a "substantial binding obligation" to expend at least five percent (5%) of the bond proceeds without contingencies (Treas. Reg. §1.148-2(e)(2)(i)(B)).
- c. Due diligence test. Work on the project must proceed, and bond proceeds must be spent, with due diligence to completion (Treas. Reg. §1.148-2(e)(2)(i)(C)).

1.12.1.1 The temporary period is three (3) years unless the capital project for which the Bonds are issued involves a substantial amount of construction expenditures, in which case

the temporary period may be extended to five (5) years; provided however, both the school district and a licensed architect or engineer certify that the longer period is necessary to complete the capital project.

.2 Rebate requirement. Section 148(f), I.R.C., provides that excess arbitrage earnings on all gross bond proceeds must be paid to the federal government at five (5) year intervals and at the retirement of all bonds or notes. "Excess arbitrage earnings" are defined generally as the aggregate investment income on their investments in excess of the yield on the bonds or notes, plus any earnings on such excess. The four general exceptions to the rebate requirement are as follows:

- a. Small issuer exception. Section 148(f)(4)(D), I.R.C., sets forth the most commonly used rebate exception (the "small issuer" exception) which exempts a school district from rebate if the aggregate face amount of all of its tax-exempt securities during the calendar year (other than certain current refundings) is not reasonably expected to exceed five million dollars (\$5,000,000). For obligations issued after December 31, 2001, The Economic Growth and Tax Relief Reconciliation Act of 2001 increased the five million dollar (\$5,000,000) small issuer exception to an amount equal to the lesser of fifteen million dollars (\$15,000,000) or so much of the aggregate face amount of the securities as are attributable to financing the construction of public school facilities.
- b. 6-month expenditure exception. Section 148(f)(4)(B), I.R.C., provides another rebate exception, although of limited utility, is the blanket exception from rebate if all gross bond proceeds, except proceeds held in a bona fide debt service reserve fund, are expended within six (6) months after issuance of the bonds or notes with certain retainage exceptions (I.R.C. §148(f)(4)(B)).
- c. 18-month expenditure exception. Treas. Reg. §1.148-7(d) provides an exception to rebate which may be valuable to a school district whose project is (a) too large to meet the small issuer exception, and (b) not at least seventy-five percent (75%) construction (see below). A bond or note issue will not be subject to rebate if the proceeds of the securities are spent on the project according to the following schedule: fifteen percent (15%) within six (6) months after issuance; sixty percent (60%) within twelve (12) months after issuance; and one hundred percent (100%) within eighteen (18) months after issuance, with certain retainage exceptions.
- d. 24-month construction bond exception. The fourth general rebate exception, and one very useful for school districts, is the construction bond exception (Section 148(f)(4)(C)(v), I.R.C.). In general, if at least seventy-five percent (75%) of the proceeds of a bond or note issue (including investment earnings) are to be spent on construction expenditures, such bond or note issue will not be subject to rebate if the proceeds of the securities are spent according to the following schedule: ten percent (10%) within six (6) months after bond issuance; forty-five

percent (45%) within twelve (12) months after issuance; seventy-five percent (75%) within eighteen (18) months after issuance; and one-hundred percent (100%) within twenty-four (24) months after issuance, with certain retainage exceptions.

Failure to meet one of the expenditure schedules would have one of two possible outcomes which the school district must elect at the time the bonds or notes are issued. The school district could elect to comply with the traditional rebate requirements, or it could elect to pay a penalty. The penalty is calculated and payable semiannually, and is equal to the product of one and one-half percent (1.5%) times the excess unspent proceeds at each semiannual period.

1.12.1.3 Hedge Bonds Another issue with respect to the expenditure of the proceeds of the Bonds of a school district is whether such bonds will constitute "hedge bonds". Section 149(g) of the Internal Revenue Code defines a "hedge bond" as a bond which is part of an issue unless the issue satisfies the following two-part test:

- i. The issuer reasonably expects that eighty-five percent (85%) of the proceeds of the bonds will be spent within three (3) years from the date the bonds are issued and;
- ii. Not more than fifty percent (50%) of the proceeds of the bonds are invested in nonpurpose investments having a substantially guaranteed yield for four (4) years or more.

Interest on a hedge bond is not tax exempt unless the school district meets the following requirements with respect to such hedge bond:

- a. Payments of costs of issuance for such bonds are not contingent;
- b. At least ninety-five percent (95%) of the costs of issuance are paid within 180 days from the date of issuance;
- c. The school district reasonably expects to spend ten percent (10%) of the proceeds within one (1) year, thirty percent (30%) of the proceeds within two (2) years, sixty percent (60%) of the proceeds within three (3) years and eighty-five percent (85%) of the proceeds within five (5) years, all from the date the bonds are issued.

The Internal Revenue Code provides that, if it is reasonably expected that the proceeds of the hedge bonds will be spent over a reasonable construction schedule, the Secretary of the Treasury, may at the request of a school district, treat the threshold spending requirements as having been met with respect to a portion of an issue of bonds used for a construction project having a construction period in excess of five (5) years. According to the legislative history, Section 149(g) of the Internal Revenue Code was added to: (i) prevent premature issuance of tax-exempt bonds to obtain lower interest rates than those in the future if interest rates increase; and (ii) limit unnecessary tax exempt bond issues.

.3 Reimbursement of prior expenditures. To qualify as an expenditure of bond or note proceeds for federal tax law purposes, a reimbursement of moneys advanced before issuing securities for expenses associated with the project must meet three requirements:

- a. the school district must declare, in writing (official intent), its reasonable intent to reimburse the expenditures not later than sixty (60) days after the payment of the expenditures that are to be reimbursed (Treas. Reg. §1.150-2(d)(1));
- b. the allocation of reimbursement bond proceeds to expenditures must take place by the required time (generally on or before the later of the date eighteen (18) months after the expenditure was paid or the date eighteen (18) months after the property was placed in service (but not later than three (3) years after the expenditure is paid)) (Treas. Reg. §1.150-2(d)(2))<sup>1</sup>; and
- c. the reimbursed expenditures must be capital expenditures (Treas. Reg. §1.150-2(d)(3)).

Generally, preliminary expenditures (such as architectural, engineering, survey, note or bond issuance and other similar costs) are permitted to be reimbursed without compliance with the official intent requirement for federal tax law purposes (Treas. Reg. §1.150-2(f)(2)).

A related Ohio law issue is whether bond or note proceeds may be transferred to the school district's general fund to reimburse the general fund for moneys advanced for the project before issuing securities. Such transfers are permitted if there has been a declaration of intent to reimburse either via a resolution or other discussion of such intent "on the record".

#### 1.12.2 Private Use.

The interest exemption provided by Section 103(a), I.R.C. will be lost if the notes or bonds are deemed private activity bonds.

A "private activity bond" is a note or bond that satisfies either the "private business use test" or the "private loan financing test." The private business use test is satisfied if: (a) more than ten percent (10%) of the bond proceeds are used in the trade or business of any person other than a governmental unit, and (b) the payment of the principal and interest on the bonds or notes representing more than ten percent (10%) of the total issue is secured by or derived from property to be used in the trade or business of non-governmental persons. If the private business use of a facility is not related to the government use of such facility or if the related private business use of the facility is disproportionate to the government use, then five percent (5%) is substituted for ten percent (10%) in each of the places it appears in the prior sentence.

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<sup>1</sup>For securities that satisfy the small issuer exception (discussed above), the eighteen (18) month limitation is changed to three (3) years (Treas. Reg. §1.150-2(d)(2)(i)).

The ownership or lease of bond-financed property by a private party constitutes private business use. In addition, management or service contracts between a school district and a private party relating to bond-financed property constitutes private business use, unless such contracts are structured within I.R.C. guidelines. Other types of contracts and arrangements conveying to private persons special legal entitlements to bond proceeds or bond-financed property may also create private business use. Generally, use of bond-financed property by a member of the general public on a first-come, first-serve basis, even if a user fee is charged, would not constitute private business use.

The private loan financing test is satisfied if the bond or note proceeds are used to make loans to any non-governmental person in excess of the lesser of five percent (5%) of the proceeds of the issue or five million dollars (\$5,000,000).

### 1.12.3 Bank Qualification.

Section 265(b)(3), I.R.C., provides that certain financial institutions get a deduction for eighty percent (80%) of that portion of the financial institution's interest expense allocable to interest on tax exempt securities, which could result in a lower interest rate on such securities. A school district may designate its bonds or notes as "bank-qualified" if the aggregate amount of all of its tax-exempt debt issued during the calendar year is not reasonably expected to exceed \$10,000,000 (this \$10,000,000 limit was raised to \$30,000,000 during 2009 and 2010 by the American Recovery and Reinvestment Act).

### 1.12.4 Practical Considerations Regarding Federal Tax Law.

Federal income tax considerations are often complex but are critical in preserving the federal income tax exemption on interest on the bonds or notes and in maximizing investment earnings on bond or note proceeds. Bond counsel should be regularly consulted regarding tax implications as financings are structured. Nevertheless, while tax implications are important, they should not be permitted to completely overshadow other important matters such as the desired construction schedule, timing a bond sale to take advantage of desirable market conditions, etc.

**VERSION ONE**  
**R.C. 133.18**  
***(Voted Bonds)***

**AFFIRMATIVE VOTE IS NECESSARY FOR PASSAGE**

Shall bonds be issued by the XYZ School District, XYZ County, Ohio for the purpose of [insert purpose clause] in the principal amount of \$\_\_\_\_\_, to be repaid annually over a maximum period of \_\_\_\_ years, and an annual levy of property taxes be made outside the ten-mill limitation, estimated by the county auditor to average over the repayment period of the bond issue \_\_\_\_ (\_\_\_\_) mills for each one dollar of tax valuation, which amounts to \_\_\_\_ (\$.\_\_\_\_) cents for each one hundred dollars of tax valuation, commencing in \_\_\_\_, first due in calendar year \_\_\_\_, to pay the annual debt charges on the bonds, and to pay debt charges on any notes issued in anticipation of those bonds?

	FOR THE BOND ISSUE
	AGAINST THE BOND ISSUE

**VERSION TWO**  
**R.C. 3318.06<sup>1</sup>**  
***(OSFC Voted Bonds)***

**AFFIRMATIVE VOTE IS NECESSARY FOR PASSAGE**

Shall bonds be issued by the XYZ School District, XYZ County, Ohio to pay the local share of school construction under the State of Ohio Classroom Facilities Assistance Program in the principal amount of \$\_\_\_\_\_, to be repaid annually over a maximum period of \_\_\_\_ years, and an annual levy of property taxes be made outside the ten-mill limitation, estimated by the county auditor to average over the repayment period of the bond issue \_\_\_\_ (\_\_\_\_) mills for each one dollar of tax valuation, which amounts to \_\_\_\_ (\$.\_\_\_\_) cents for each one hundred dollars of tax valuation to pay the annual debt charges on the bonds and to pay debt charges on any notes issued in anticipation of the bonds?

**and**

Shall an additional levy of taxes be made for a period of twenty-three (23) years to benefit the XYZ School District, XYZ County, Ohio the proceeds of which shall be used to pay the cost of maintaining the classroom facilities included in the project, at the rate of one-half (0.50) mill for each one dollar of valuation?

**and/or**

Shall bonds be issued by the XYZ School District, XYZ County, Ohio to pay costs of acquiring a site for classroom facilities<sup>2</sup> under the State of Ohio Classroom Facilities Assistance Program in the principal amount of \$\_\_\_\_\_ to be repaid annually over a maximum period of \_\_\_\_\_ years, and an annual levy of property taxes be made outside of the ten-mill limitation, estimated by the County Auditor to average over the repayment period of the bond issue \_\_\_\_ (\_\_\_\_) mills for each one dollar of tax valuation, which amount to \_\_\_\_ (\$.\_\_\_\_) cents for each one hundred dollars of tax valuation to pay the annual debt charges on the bonds, and to pay debt charges on any notes issued in anticipation of those bonds?<sup>3</sup>

**and**

Shall an additional levy of taxes outside the ten-mill limitation be made for the benefit of the XYZ School District, XYZ County, Ohio for the purpose of acquiring a site for classroom facilities in the sum of \$\_\_\_\_\_ estimated by the County Auditor to average \_\_\_\_ (\_\_\_\_) mills for each one hundred dollars of valuation for a period of \_\_\_\_\_ years?

	FOR THE BOND ISSUES AND TAX LEVIES
	AGAINST THE BOND ISSUES AND THE TAX LEVIES

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1 – O.R.C. 3318.062 also provides that a school district participating in CFAP may issue bonds incrementally to pay for the project.  
2 - Bonds under this section also are used to finance "locally funded initiatives."  
3 - Acquisition of CFAP sites may also be funded through the passage of a permanent improvement levy.

**VERSION THREE**  
**R.C. 5705.218**

*(Bond Issue Combined with Levy)*

**AFFIRMATIVE VOTE IS NECESSARY FOR PASSAGE**

Shall the XYZ School District, XYZ County, Ohio be authorized to do the following:

(1) Issue bonds for the purpose of [insert purpose clause/paying the local share of school construction under the State of Ohio Classroom Facilities Assistance Program], including [insert local initiative purpose clause if applicable] in the principal amount of \$\_\_\_\_\_, to be repaid annually over a maximum period of \_\_\_\_\_ ( ) years, and levy a property tax outside the ten-mill limitation, estimated by the County Auditor to average over the bond repayment period \_\_\_\_ ( ) mills for each one dollar of tax valuation, which amounts to \_\_\_\_\_ ( ) cents for each \$100 of tax valuation to pay the annual debt charges on the bonds, and to pay debt charges on any notes issued in anticipation of those bonds?

**and/or**

(2) Levy an additional property tax to provide funds for the acquisition, construction, enlargement, renovation, and financing of permanent improvements, [including infrastructure improvements,] at a rate not exceeding \_\_\_\_\_ ( ) mills for each one dollar of tax valuation, which amounts to \$.\_\_\_\_\_ ( ) cents for each \$100 of tax valuation, for [\_\_\_\_ years<sup>1</sup>/a continuing period of time]?

**and/or**

(3) Levy an additional property tax to pay current operating expenses at a rate not exceeding \_\_\_\_\_ ( ) mills for each one dollar of tax valuation, which amounts to \$.\_\_\_\_\_ ( ) cents for each \$100 of tax valuation, for [\_\_\_\_ years/a continuing period of time]?

	FOR THE BOND ISSUE AND LEVY
	AGAINST THE BOND ISSUE AND LEVY

**VERSION FOUR**  
**R.C. 5748.08**

*(Bond Issue Combined with Income Tax)*

**AFFIRMATIVE VOTE IS NECESSARY FOR PASSAGE**

Shall the XYZ School District, XYZ County, Ohio be authorized to do both of the following:

(1) Impose an annual income tax of \_\_\_\_\_ percent ( )% on the [insert "school district income of individuals and of estates" or "earned income of individuals residing in the school district"] for [insert "\_\_\_\_ ( ) years" or "a continuing period of time"], beginning [month and day] 20\_\_, for the purpose of [insert purpose clause]?

(2) Issue bonds for the purpose of [insert purpose clause], in the principal amount of \_\_\_\_\_ dollars (\$\_\_\_\_\_), to be repaid annually over a maximum period of \_\_\_\_\_ ( ) years, and levy a property tax outside the ten-mill limitation estimated by the county auditor to average over the bond repayment period \_\_\_\_ ( ) mills for each one dollar of tax valuation, which amounts to \_\_\_\_\_ cents (\$.\_\_\_\_) for each \$100 of tax valuation, to pay the annual debt charges on the bonds, and to pay debt charges on any notes issued in anticipation of those bonds?

	FOR THE INCOME TAX AND BOND ISSUE
	AGAINST THE INCOME TAX AND BOND ISSUE

<sup>1</sup> O.R.C. 5705.218(I) provides that an ELPP school district choosing to fund maintenance up front may have a 23-year levy.

