

MEMORANDUM

To: Rye City Council
From: Rye City Finance Committee
Date: August 12, 2010
Re: Analysis of Rye's Charter Bond Limitations

David Mullane, Norm MacMaster and Arthur Stampleman are the members of the Charter Limitations Task Force of the Rye City Finance Committee. The Task Force was organized in response to Mayor French's request of the Finance Committee to examine Rye City's Charter Bond Limitations and report back to the City Council on our findings. This Memorandum summarizes the conclusions of a majority of the Finance Committee.

For the reasons outlined in the Memorandum we recommend that the Charter Bond Limitations not be changed. We also recommend, however, that the City Council consider a new amendment to the Charter which will permit the Council to issue bonds (subject only to its majority vote process) to be used to fund the City's share of public improvement projects where the City receives a minimum 50% of matching federal, state or other outside funding to pay for the cost of such improvements and such matching funding sources are determined by the City Manager to be forthcoming on a timely basis.

In the Memorandum we also address various arguments with respect to which there was minority support among members of the Finance Committee in favor of changing the Charter Bond Limitations to provide more bond issuance discretion to the Council.

Legal Debt Limits:

Section C21-9 of the City of Rye Charter (the "Charter") outlines when bond referenda are required, recommended and not required. The following is a summary of the Charter's applicable provisions (in plain English), with current prior funding amount figures added where applicable.

Mandatory Referendum Required: A mandatory referendum is required for any proposed bond issuance in excess of 10% of Rye's Average Gross Annual Budget for the proceeding three years ("AGAB").

Application: For the fiscal year ending December 31, 2010 the AGAB is currently \$39,486,826. Accordingly, any proposed bond issuance in excess of \$3,948,683 is

subject to a Mandatory Referendum. Rye currently has approximately \$12,185,735 of outstanding bonds that has been issued pursuant to the mandatory referendum process.

Permissive Referendum Required: A Permissive Referendum¹ is required for any proposed bond issuance in excess of 5% (\$1,974,341) but less than 10% (\$3,948,682) of the AGAB. To determine the current Permissive Referendum threshold amounts, subtract from the 10% AGAB calculation the outstanding amount of all outstanding bonds previously issued under permissive referenda, currently \$2,306,073.²

Application: The City Council can currently adopt a resolution calling for the issuance of bonds totaling \$1,642,610 (\$3,948,682 - \$2,306,073). Unless a number of Rye's registered voters (equal to 10% of the votes cast for Governor in the last election) object to this resolution, the bonds will be issued in accordance with the City Council's vote. If the voters' objection is sustained, then the resolution must be put to a referendum.

City Council Vote: The City Council can authorize solely by resolution (i.e. without a referendum of any kind) a bond issuance for amounts less than 5% of AGAB (\$1,974,341). To determine the current City Council Vote threshold amount subtract from the 5% AGAB calculation the outstanding amount of all previous bonds issued pursuant to City Council Votes, currently \$1,956,341.³

Application: The City Council can currently adopt a resolution for the issuance of bonds totaling \$18,000 solely by a City Council Vote. Until last month, the City Council had \$1,390,040 available under this threshold. All but approximately \$18,000 of this \$1,390,040 was authorized by the City Council recently for various projects, however.

¹ A Permissive Referendum gives registered voters the ability to challenge an action by the City Council (such as a resolution to issue bonds). If a number of registered voters, equal to 10% of the number of votes cast for Governor by Rye voters in the last election, sign a petition to require a referendum on the matter and submit it to the City Council within 45 days of the resolution date, a referendum must be held for the voters to approve the City Council's action. If the referendum fails (i.e. the voters do not approve the City Council's action), then the action cannot be taken (e.g. the City could not issue bonds). From a practical application perspective, we contend that a presumption of validity is given to the actions of the City Council; and it takes the affirmative action of a meaningful number of registered voters to start a process to unwind the action taken by the City Council.

² The aggregate funding limitations 'look back' to prior issuances under the permissive referendum process is similar to the operation of a revolving line of credit. Prior draw-downs on the line must be considered when one is considering an additional drawdown. As prior draw-downs under the line of credit are paid back, the line 'resets' accordingly.

³ The same aggregate funding limitations 'look back' process described in footnote two above applies to bonds authorized by City Council Vote.

Charter’s Non-Application to Certain Bond Resolutions:

The Charter does not apply to the following bond resolutions, thereby allowing the Council to act only through its own resolution, as follows:

Judgments: Issuance of bonds where the bond proceeds are used for the payment of various legal, administrative and quasi judicial judgments against the City

Environmental Infrastructure Needs: Issuance of bonds sold to New York State Environmental Facilities Corporation (e.g. to fund the purchase/construction of sewer drains and/or other environmental infrastructure needs).

Mandatory Legal Compliance: Issuance of bonds where the bond proceeds are used to comply with mandated Federal, State or County laws.

Capital Improvements/Equipment with Local Assessment: Issuance of bonds used to make capital improvements or purchase equipment where the expense is borne by local assessment on lots/land deriving the benefit thereof.

Public Safety Improvement: Issuance of bonds where the bond proceeds are used for public safety improvement (e.g. fire, police, ambulance, building inspection subject to a \$1,000,000 annual cap and a \$2,500,000 aggregate cap. The City Council has authorized funding of \$1,623,902 under the public safety improvement exception, including \$1,230,000 this year. Accordingly, there remains \$876,097 that can be utilized (in 2011 if necessary).

A Recommendation For A “Public Improvements” Charter Amendment:

We recommend that an amendment to the Charter be made providing the Council with the authority, pursuant to majority vote, to issue bonds for the following purpose:

Public Improvement Projects with Matching Funding: Issuance of bonds to fund the City’s share of public improvement projects [to be defined] where the City receives a minimum 50% of matching federal, state or other outside funding to pay for the cost of such improvements and such matching funding sources are determined by the City Manager to be forthcoming on a timely basis. We propose that this amendment be subject to a \$400,000 annual cap and a \$1,000,000 aggregate cap.

The intent behind this proposed Charter amendment is to enable the City to avail itself of “matching funds” during times, like the present, when it has less flexibility under the Charter due to the aggregate funding limitations. For example, the City Council could utilize the public improvements amendment to the Charter to avail itself of CHIPS funding to be used to pave/repair roads.

We caution, however, that given the well-publicized financial difficulties that New York State is experiencing, and Rye’s poor recent experiences with respect to the timing of the receipt of matching funds promised by New York State, this

exception should be carefully considered. If this new exception to the Charter is in fact implemented, it should be implemented with appropriate caution.

A Different Perspective Considered:

Before reaching the conclusions set forth in this memorandum, the majority of the Finance Committee members carefully considered the following arguments made by a minority of the Finance Committee in favor of changing the Charter to provide more flexibility to the City Council as follows:

- The Charter Calculations are Too Complex
- The Calculation of Some of the Charter’s Aggregate Funding Limitations are Illogical
- City Councils View Permissive Referenda as Equivalent to Mandatory Referenda, and Therefore the Permissive Referendum Process Should be Eliminated from the Charter
- Rye’s Tax Base can Tolerate More Debt
- The Charter Limitations Limit Ability to Make Capital Expenditures
- It is Too Restrictive to Hold Bond Referenda in November

The Charter Calculations are Too Complex:

One argument against the current guidelines is that they are “too restrictive” and require “a complex set of calculations”. We disagree. Here is a “Cliff Notes” description of the key guidelines that can be easily understood by taxpayers:

- Mandatory referenda: Any bond issuance proposal that exceeds 10% of the City’s annual budget (averaged over three years) must be approved by taxpayer vote. Currently this means any bond issuance proposal in excess of approximately \$4,000,000.
- Permissive referenda: The Council may approve bond issuance proposals for amounts between 5 and 10% of the City’s average budget by a simple majority vote subject to two conditions:
 - Taxpayers may challenge the Council vote through a petition submitted within 45 days of the vote and signed by a number of voters equal to 10% of the Rye votes cast for Governor in the last election. If so challenged, the proposal goes to a referendum.
 - The amount available for permissive referenda is reduced by the aggregate amount of unretired bonds issued this way in the past.
- Bonds issued pursuant to Council vote: By a simple majority vote, the Council can approve bond issuance proposals of less than 5% of the City’s average budget, less the aggregate of unretired bonds issued this way in the past.

It is our view that the Charter limitations are hardly overly restrictive or onerous. The required calculations are simple additions and subtractions. They could be entered in an Excel spreadsheet and easily updated as necessary. It's not as if the inputs change daily, weekly or even monthly. In fact, the Comptroller's office maintains these calculations as part of its normal operating procedures.

The Calculations of Some Aggregate Funding Limitations Are Illogical:

During our deliberations reference was made to the fact that approximately \$2 million of bonds that were authorized during the period between 2000 and 2005 are currently outstanding and are deducted from the amounts that can be approved by the Council on its own or with permissive resolutions. An argument was made that it is illogical to consider these outstanding bonds determining what further amounts the Council can approve (i) on its own or (ii) subject to a Permissive Referendum, because "how" bonds "approved five to ten years ago should not be as relevant as what the City's total debt burden is immediately before or after debt is incurred." In support of the above argument, the following suggestion was proffered as a safeguard to prevent a Council from circumventing the Charter's aggregate funding limitations: "Limit the deductions in the above calculations to debt approved in the past few years, or the life of a Council, but not five years."

We believe that the above argument and accompanying suggestion subvert the clear intent of the Charter. First, unretired debt issued five or ten years ago is part of the City's total debt burden. Consequently, making reference to it is consistent with the minority (total debt) view described above. Second, the unretired debt calculations act as 'circuit breakers' governing the amount of debt issued without broad taxpayer involvement. The intent of the Charter is to have these circuit breakers kick in when prior debt issuance exceeds the designated levels.

In sum, all unretired debt is part of the City's "total debt burden" and, regardless of when it was issued or by which Council, is very relevant to the taxpayer.

City Councils View Permissive Referenda as Equivalent to Mandatory Referenda, and Therefore the Permissive Referendum Process Should be Eliminated from the Charter:

Another argument for increased Charter flexibility for the Council states that the rule requiring permissive referenda has often been treated by Councils as the same as requiring a mandatory referendum. As support for this argument it was noted that "...two mandatory recreation bond issues have been turned down by voters in the past 20 years, which may make a Council gun shy with any hint of a referendum possibility".

The proposed solution to these apparent problems is to eliminate the permissive referendum language from the Charter, thereby entrusting the City Council with (increased) authority to issue bonds using only the City Council vote procedure in amounts up to the mandatory referendum threshold (i.e. 10% of AGAB).

It is our view that two rejections in 20 years suggest that most bond referenda get approved by voters. But if in fact the Council has become gun shy about bond referenda, it is unclear how doing away with the permissive referendum procedure and making all referenda mandatory solves this problem. On the contrary, we believe that the permissive referendum procedures are an integral aspect of the Charter and their elimination for the above-described reason is unwarranted.

Rye Can Tolerate More Debt:

A database issued by New York State covering 61 cities in the State was cited as support for the argument that because Rye has much less debt on its assessed property values than other New York State communities it can be more flexible and carry more debt. It was noted in the database that Rye's debt as a percentage of full assessed property value is 0.4% versus the State average of 2.4%.

We rejected this argument for several reasons. First, we disagree with using debt as a percentage of full assessed property value as a measure of the City's debt tolerance. If we take this line of reasoning to its logical conclusion, Rye could support a debt to assessed property value (applying the State average of 2.4%) of \$175 million. That seems unrealistic.

The second problem with this line of reasoning is that full property value is not a useful statistic for comparing one community to another. On a per capital basis, full assessed property value for all the 61 cities included in the database is \$59,000 versus \$472,000 in Rye. But Rye's per capita value is inflated by the number of very large homes in our community and the City's extensive amount of waterfront property. It's fair to say that, in Rye, the difference in property value between homes in the top quintile and those in other quintiles is much greater than is the case in other communities. Here's an analogy that will clarify. If Bill Gates and Warren Buffet moved to Rye, the City's collective "wealth" would increase significantly and our per capita "wealth" would increase dramatically. But that doesn't mean that each of us was suddenly very rich and able to handle more debt.

Third, we note that Rye's debt per capita is \$1,709 versus the 61 city average of \$1,645. Lest some jump to the conclusion that because Rye is a more affluent community it can handle more debt, we note that Rye's property taxes per capita (\$1,207) are three times the 61 city average (\$397).

The Charter Limitations Limit Ability to Make Capital Expenditures:

An argument was made that the Charter limits the ability of the Council to make capital expenditures it considers essential in 2011 because (i) unreserved, undesignated fund balances which have generally been one source of capital funding have fallen due to tight budget conditions; (ii) it is difficult to raise taxes in today's current economic climate; and (iii) the Charter limits Council flexibility. In support of this argument it was noted that capital improvement projects have averaged \$5 million annually for the past five years; and the City's Capital Improvements Plan Requirements for the years 2011-2015 are \$37 million.

As previously communicated by the Comptroller's office, the August 11, 2010 Council meeting is the last meeting at which the Council can authorize a November, 2010 bond referendum relating to the capital expenditures the Council deems essential in 2011. As for the claim that the magnitude of capital improvements projects over the past five years and the anticipated capital improvement projects over the next five years (as set forth 2011-2015 Capital Improvements Plan) argues for more Council flexibility, we believe that in fact it argues otherwise. We believe these facts call for more taxpayer involvement in the decision making process-- not less⁴.

Holding Bond Referenda in November is Unduly Restrictive:

Several Finance Committee members commented on the Council policy that City bond referenda be held on election Tuesday in November (other than for certain specified exceptions). We remind the Council that this policy is not part of the City Charter and was established by a prior Council resolution. As such, it can be changed at any time by Council vote.

Conclusion:

It is true that the City's Charter guidelines regarding bond issuance differ from many other communities. The result has been more taxpayer involvement in Rye bond issuance decisions than is the case elsewhere. We believe that the balance struck between Council discretion and taxpayer involvement has been to the benefit of the City and the taxpayers over the years.

Our analysis of the Charter indicates that it is a very flexible document that in some ways provides the citizens of Rye with a 'best of both worlds' scenario. As stated above, the Charter limits the amount of bonds that can be authorized by a City Council unilaterally. At the same time, the City Council is given tremendous flexibility to issue bonds without being burdened by the mandatory referenda process. As indicated above, under the Charter the City Council has the ability to issue (outside of the mandatory referendum procedures):

- \$1,974,341 of bonds (5% of AGAB) pursuant to its own vote;
- \$1,974,341 of additional bonds (more than 5% but less than 10% of AGAB) subject to the permissive referendum procedure;
- \$2,500,000 of bonds under the public safety exception;
- Unlimited amount of bonds to pay legal judgments;

⁴ Reference should be made to the above-described Charter exception which allows the Council to issue an unlimited amount of bonds if sold to New York State Environmental Facilities Corporation (e.g. to fund the purchase/construction of sewer drains and/or other environmental infrastructure needs).

- Unlimited bonds sold to New York State Environmental Facilities Corporation (e.g. to fund the purchase/construction of sewer drains and/or other environmental infrastructure needs);
- Unlimited bonds to pay for capital improvements/equipment where expense is borne by assessment on lots/land deriving benefit thereof;
- Unlimited amount of bonds to comply with various federal, state and local laws; and
- [Subject to Council's approval] An additional \$1,000,000 of bonds to pay for the City's share of public improvement projects which are subject to the receipt of matching funds.

In addition, we note that the Charter's limits only apply to bond issuance; and do not address borrowings undertaken by the Council in other formats including, without limitation, the following:

- debt for seller-financed long term obligations incurred, e.g. the (over \$6 million) debt incurred when the City purchased 1037 Boston Post Rd.
- long term capitalized leases entered into by Council, which may be viewed as the capital equivalent of debt.
- a proposal for the issuance of \$4,550,000 of Revenue Anticipation Notes

The Finance Committee would be willing to develop guidelines to cover these additional borrowings if the Council wishes us to do so.

At present the Charter's circuit breakers, which require unretired bonds to reduce the amount of bonds that can be issued by Council vote or through a permissive referendum, are kicking in. While this may require more use of mandatory referenda, the City's ability to issue bonds, subject to taxpayer approval, is not restricted. We see no persuasive argument to change the Charter guidelines.