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ATTORNEY GENERAL OPINION NO. 86- 112

Norman E. Gaar
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Overland Park, Kansas 66210

Re: Bonds and Warrants--Refunding Bonds--Conditions and
Limitations; Refinancing Construction Accounts

Synopsis: A school district which has money remaining in a construction account funded with proceeds of a bond issue authorized by K.S.A. 72-6761 may, in conjunction with the issuance of K.S.A. 1985 Supp. 10-427 et seq. general obligation bonds designed to refund the outstanding bonds, transfer the money in the construction account to an escrow (as described in K.S.A. 10-427a) pledged for the payment of principal and interest on the outstanding bonds. A portion of the proceeds of the issue not required for the escrow may then be transferred to replenish the construction account. The school district's original authority to issue general obligation bonds pursuant to K.S.A. 72-6761 together with its authority to refund its outstanding general obligation bonds pursuant to K.S.A. 1985 Supp. 10-427 permits such a transaction to be accomplished without an election or a repetition of the authority required by K.S.A. 72-6761. Pursuant to K.S.A. 1985 Supp. 10-427a the issuance of such bonds will not increase the school districts indebtedness for the purpose of calculating statutory debt limitations. Cited herein: K.S.A. 10-117; K.S.A. 1985 Supp. 10-120; K.S.A. 10-427; 10-427a; K.S.A. 72-6761.

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Dear Mr. Gaar:

As bond counsel for the Board of Education of Unified School District No. 231, Johnson County, Kansas, you seek an Attorney General opinion on behalf of the District regarding a method of refinancing which the District hopes to use in the near future. You state the District's question as follows: "Can the School District use money held in a K.S.A. 72-6761 authorized bond issue construction account, along with other money, to fund an escrow for the payment of outstanding bonds and issue bonds without an election to replenish the construction account?"

You inform us that the District is considering refunding its outstanding general obligation bonds pursuant to K.S.A. 10-427 et seq. in order to achieve interest cost savings and provide a more economical program for retiring the District's debt. The District presently has three series of bonds outstanding. The Series A, 1977 bonds and the Series A, 1985 bonds were issued pursuant to K.S.A. 72-6761. The Series B, 1985 bonds are refunding bonds issued pursuant to K.S.A. 1985 Supp. 10-427 to refund the two earlier issues. At this time a portion of the proceeds of the Series A, 1985 bonds remain in a construction account. The District now proposes to issue general obligation refunding bonds to refund the Series B, 1985 bonds in order to achieve further cost savings on its debt service obligations. It is our understanding that due to various intricacies of the federal tax law, even greater cost savings for the District will occur if the funds in the Series A, 1985 construction account, along with other available funds and a portion of the proceeds of the 1986 bonds to be issued, may be placed in escrow for the payment of principal and interest on the refunded Series B, 1985 bonds. The remaining portion of the 1986 bond proceeds would be used to replace the money transferred to escrow from the Series A, 1985 construction account.

It is the opinion of the Board of Education that it has the statutory authority to refund the District's debt as described without repeating the steps prescribed by K.S.A. 72-6761 to replenish the construction fund, and that such a refinancing would not increase the District's general obligation debt for the purpose of calculating its statutory debt limitation. You ask whether the Attorney General concurs with these conclusions. Our review of the Kansas statutes relevant to

this inquiry reveals neither a specific prohibition nor authorization of the refinancing proposed by the District. It would appear, however, that the refinancing, structured as described earlier, can be viewed as within the District's statutory authority to both issue general obligation bonds and to refund any outstanding bonds.

K.S.A. 72-6761 permits a school district to issue general obligation bonds for the acquisition, construction, equipping, furnishing, repair or remodeling of buildings to be used for school district purposes. No bonds exceeding the principal amount of \$20,000.00 may be issued unless first authorized by a vote of the qualified electors of the district in an election held pursuant to K.S.A. 1985 Supp. 10-120. When the District has issued bonds under this statute it is then authorized and empowered by K.S.A. 1985 Supp. 10-427, as are all Kansas municipalities (see K.S.A. 10-101), to refund its outstanding bonds. K.S.A. 1985 Supp. 10-427 further provides that the municipality may issue refunding bonds for the purpose of refunding its outstanding bonds and that:

"The principal amount of any issue of any refunding bonds shall not exceed the aggregate amount of: (a) The principal amount of the issue or issues or part thereof being refunded; (b) the amount of any interest which has accrued or will accrue to the date of payment of the bonds being refunded; (c) the amount of any redemption premium required; (d) expenses of the municipality deemed by the governing body to be necessary for the issuance of the refunding bonds; and (e) in the event the proceeds from the sale of the refunding bonds are to be placed in escrow and invested, the interest to accrue on the refunding bonds from the date of delivery to the first or any subsequent available redemption date or dates selected by the governing body of the municipality, or to the date or dates of maturity, whichever is determined by the governing body to be most advantageous or necessary to the municipality."

The governing body of an issuer has both the authority and the responsibility to determine whether a refunding will be beneficial to the issuer and, if so, how such a refunding may

best be accomplished. The statutes do not require that such action be authorized by the voters, nor that it is subject to protest by the voters. As noted above, the generally understood purpose of a refunding is to provide the issuer with the ability to structure its outstanding debt in the most efficient and economical manner. In most instances the result of a refunding is to save the issuer significant sums of money on its debt service obligations. In this sense we believe that the authority to refund may be viewed as a part the District's overall authority and responsibility to accomplish the projects for which it is authorized to issue general obligation bonds in the most efficient and economical manner possible.

K.S.A. 1985 Supp. 10-427a provides the following guidance regarding the issuance of refunding bonds to refund outstanding bonds.

"(a) Refunding bonds issued under the authority of K.S.A. 10-427, and amendments thereto, may be sold or exchanged for the bonds being refunded either as a whole or in installments at any time either at, before or after the maturity of the bonds being refunded. Such bonds shall be exempt from statutory limitations of bonded indebtedness and shall not be included in computing the total bonded indebtedness of the municipality for the purpose of applying any statute limiting the bonded indebtedness of the municipality.

"(b) If refunding bonds are sold more than six months prior to the maturity or earliest prior redemption date of the bonds being refunded, the proceeds derived from the sale, together with any other moneys on hand, shall be placed in escrow under a trust agreement with a Kansas bank having full trust powers. The proceeds and moneys shall be invested in direct obligations of, or obligations the principal of and the interest on which are unconditionally guaranteed by, the United States of America and which shall mature or be subject to redemption by the holders thereof not later than the respective

dates when the proceeds of the obligations together with the interest accruing thereon and any other moneys or investments held in escrow will be required for the purpose intended. The trust agreement shall pledge or assign the moneys and investments held in trust for the payment of the principal of and the interest on the bonds being refunded and any redemption premium and shall contain provisions for protecting and enforcing the rights and remedies of the holders of the bonds." (Emphasis added.)

As is apparent from the emphasized language, in an advance refunding, the statute contemplates the use of funds other than the proceeds of the refunding bonds to fund the escrow necessary for the payment of principal and interest on the refunded bonds. The statute does not designate the source of "other moneys on hand" but presumably refers to any moneys lawfully available for that purpose.

We are not unmindful that a strict construction of K.S.A. 1985 Supp. 10-427a could be argued to require that all proceeds of refunding bonds issued under the circumstances there described be placed in escrow under a trust agreement for payment of the refunded bonds. Such a construction would thus preclude the use of a portion of the bond proceeds to replenish a construction fund which, in turn, has been placed in escrow to be used for the payment of principal and interest on refunded bonds. We believe that under the present circumstances such a strict construction of the statute is neither warranted nor required.

It is apparent both from the statute and common practice that all the proceeds of a refunding issue are not required to be placed in escrow solely for the payment of the refunded bonds. An issuer is permitted to use a portion of the refunding bonds for the payment of the cost of issuance and such proceeds are not placed in the escrow required by K.S.A. 1985 Supp. 10-427a despite the fact that statute presumably refers to all proceeds of such bonds.

Although the use of such proceeds to replenish a construction fund is somewhat different and likely to involve larger sums we do not believe that K.S.A. 1985 Supp. 10-427a should be read to prohibit such a transaction as it may be viewed both as part the original bond issue which funded the construction

fund and of the refunding of that issue. In other words, it is our opinion that the restrictions found in K.S.A. 1985 Supp. 10-427a(b) are intended to prevent the diversion of refunding bond proceeds to purposes unrelated to the accomplishments of a successful refunding and to prevent the refunding transaction from failing to provide for the payment of the refunded bonds.

Similarly, we do not believe that the proposed refinancing runs afoul of K.S.A. 10-117, which prohibits the diversion of proceeds of a bond issue to any purpose than that for which the bond issue was intended. If the District's authority to issue bonds to accomplish the purposes permitted by K.S.A. 72-6761 is considered in conjunction with its authority to refund those bonds to accomplish cost savings pursuant to K.S.A. 1985 Supp. 10-427, the proposed refinancing falls well within the District's statutory authority. The transfer of the construction fund, i.e., proceeds of the original issue, to the escrow to refund the original issue is clearly concerned with the most economical accomplishment of the original project. The construction money is not diverted to any unrelated purpose and the construction fund will be simultaneously replenished to continue the project without creating further indebtedness for the District.

This is true because the refunding bonds are, by statute, exempt from statutory limitations of bonded indebtedness and thus not included in computing total bonded indebtedness of a municipality. See 10-427a. The 1986 bonds simply replace the debt defeased by the refunding transaction. This is not altered by the use of a portion of the 1986 bond proceeds to replace the construction fund since the debt represented by the construction fund is refunded and defeased by the proposed refinancing.

In our opinion, the initial authority to issue general obligation bonds for some lawful purpose, read in conjunction with an issuer's authority to refund its outstanding bonds, permits an issuer to use available funds and authority to accomplish the project and the financing/refinancing thereof in the most efficient and economical manner. Under the plan proposed by the District, the purpose of a successful refunding is not defeated by the transfer of the construction fund to the escrow for the refunded bonds and the replacement of the construction fund with proceeds of the 1986 bonds. The escrow will be fully funded and pledged for the payment of principal and interest on the outstanding bonds. The purpose for which the outstanding bonds were authorized and issued

will be accomplished without creating further indebtedness. Thus, neither the purpose of the refunding bond issue nor the purpose of the original issuance pursuant to K.S.A. 72-6761 will be defeated by the proposal. In fact, due to the vagaries of federal tax law, for a short time, the proposed transaction will substantially enhance the savings accomplished by the refunding thus reducing the overall expense of the original project to the issuer.

It is our opinion that the proposed refinancing is well within the District's statutory authority as described in this opinion. Obviously any such transaction which diverted bond proceeds from the lawful purposes of accomplishing the project and refunding the bonds issued for the project would run afoul of K.S.A. 10-117 and 10-427a. We find no such difficulty, however, with the refinancing proposed by the District as described in your letter.

Very truly yours,



ROBERT T. STEPHAN
Attorney General of Kansas



Mary F. Carson
Assistant Attorney General

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