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STATEMENT OF THE CASE

The City of Panama City Beach, Florida (the "City") filed on January 14, 1987 its Complaint pursuant to Chapter 75, Fla. Stat. (1985), for validation of its \$300,000,000 City of Panama City Beach, Florida Investment Revenue Bonds (the "Bonds"), Circuit Civil No. 87-104 (Appendix 2). The Complaint alleged that on January 8, 1987 the City adopted its Resolution No. 87-2 determining to issue the Bonds for the purpose of realizing an investment profit to be utilized by the City for various municipal purposes. (Appendix 2, p.2).

The Circuit Court issued its Order to Show Cause on January 14, 1987 (Appendix 3) and the State filed its Answer on February 18, 1987 (Appendix 4). Hearing on the Order to Show Cause was held on February 18, 1987. A transcript of the hearing is attached as Appendix 5.

The Final Judgment of Validation was filed February 20, 1987 and is the order herein sought to be reviewed (Appendix 1).

STATEMENT OF THE FACTS

The City adopted its Resolution No. 87-2 for the stated purpose of issuing not-to-exceed \$300,000,000 of Bonds, the net proceeds of which, totalling approximately \$295,500,000 (App. 5, p. 20), will be placed in trust pursuant to a Trust Indenture between the City and a corporate trustee (the "Indenture") (App. 2, Exhibit A to Exhibit 1, p. 15). The trustee will invest the Bond proceeds as the City directs in the Indenture in an investment contract having a guaranteed rate of return. (App. 5, p. 15). The principal amount invested in the investment contract, together with the guaranteed earnings thereon will be pledged as security to owners of the Bonds and will constitute the sole method of repayment of principal of and interest on the Bonds (App. 5, p. 16). No other revenues of the City are obligated for repayment of the Bonds under Resolution No. 87-2 or the Indenture. (App. 5, p. 17, 23-24). Interest paid to owners of the Bonds will not be exempt from federal income taxation. (App. 5, p. 15).

The testimony at the validation hearing showed that the rate of interest on the Bonds is expected to be approximately 1/2 of 1% less than the interest rate on the investment contract, resulting in a profit to the City of approximately \$5 per \$1,000 of Bonds issued, or \$1.5 million when reduced to present value. (App. 5, p. 15).

The City has determined in Resolution No. 87-2 to apply these investment earnings to the "Project", defined in Resolution 87-2 as municipal park and recreational facilities, funding of municipal self-insurance reserves or other municipal purposes determined by subsequent resolution of the City. (App. 2, Exhibit 1, p. 3).

Witnesses for the City testified that the investment contract will be entered into between the trustee and an insurance company or other institution with a sufficient credit rating to obtain a rating of "A" or better for the Bonds by a nationally recognized bond rating agency (App. 5, p. 23).

SUMMARY OF ARGUMENT

The Court erred in validating the Bonds because the principal activity undertaken by the City with proceeds of the Bonds, i.e. the investment of Bond proceeds in an investment contract, does not constitute a municipal function in accordance with Article VIII, Section 2, of the Florida Constitution and the pledging of such investment contract as security for repayment of the Bonds violates Chapter 166, Part II, Florida Statutes (1985) by improperly pledging municipal property.

The Court erred in validating the Bonds because the proceeds of the Bonds are not required by the terms of Resolution No. 87-2 or the Indenture to be invested in accordance with the provisions of Section 166.261, Florida Statutes (1985) governing investments of surplus public funds.

ARGUMENT

ISSUE I. THE COURT ERRED IN VALIDATING THE BONDS BECAUSE INVESTMENT OF BOND PROCEEDS IN AN INVESTMENT CONTRACT TO REALIZE A PROFIT DOES NOT CONSTITUTE A MUNICIPAL FUNCTION WITHIN THE MEANING OF ARTICLE VIII, SECTION 2 OF THE FLORIDA CONSTITUTION AND PLEDGE OF THE INVESTMENT CONTRACT AS SECURITY FOR BONDS VIOLATES CHAPTER 166, Part II, FLORIDA STATUTES (1985).

Since adoption of the 1968 Florida Constitution municipalities have been imbued with powers of "home-rule." Article VIII, Section 2 of the Florida Constitution provides:

(b) POWERS. Municipalities shall have governmental, corporate and proprietary powers to enable them to conduct municipal government, perform municipal functions and render municipal services, and may exercise any power for municipal purposes except as otherwise provided by law . . . [Emphasis supplied].

The Constitution thus mandates that no specific authorization by general law is required for a municipality to act, subject only to two basic limitations:

1. The power sought to be exercised must be a municipal function or constitute the rendering of a municipal service;

and

2. There must be no contrary or superceding legislation restricting or prohibiting the exercise of such power.

See, Lake Worth Utilities Authority v. City of Lake Worth, 468 So.2d 215 (1985); City of Miami Beach v. Fleetwood Hotel, Inc., 261 So.2d 801 (Fla. 1972)

The general law governing the issuance by municipalities of bonded indebtedness is contained in Section 166.111, Florida Statutes (1985), which provides:

The governing body of every municipality may borrow money, contract loans, and issue bonds as defined in 166.101, Florida Statutes, from time to time to finance the undertaking of any capital or other project for the purposes permitted by the state constitution and may pledge the funds, credit, property, and taxing power of the municipality for the payment of such debts and bonds. [Emphasis supplied]

The types of bonds specifically permitted are detailed in Section 166.101, Florida Statutes (1985):

(1) The term "bond" includes bonds, debentures, notes, certificates of indebtedness, mortgage certificates, or other obligations or evidences of indebtedness of any type or character.

(2) The term "general obligation bonds" means bonds which are secured by, or provide for their payment by, the pledge, in addition to those special taxes levied for their discharge and such other sources as may be provided for their payment or pledged as security under the ordinance or resolution authorizing their issuance, of the full faith and credit and taxing power of the municipality and for payment of which recourse may be had against the general fund of the municipality.

(3) The term "ad valorem bonds" means bonds which are payable from the proceeds of ad valorem taxes levied on real and tangible personal property.

(4) The term "revenue bonds" means obligations of the municipality which are payable from revenues derived from sources other than ad valorem taxes on real or tangible personal property and which do not pledge the property, credit, or general tax revenue of the municipality.

(5) The term "improvement bonds" means special obligations of the municipality which are payable

solely from the proceeds of the special assessments levied for an assessable project.

(6) The term "refunding bonds" means bonds issued to refinance outstanding bonds of any type and the interest and redemption premium thereon. Refunding bonds shall be issuable and payable in the same manner as the refinanced bonds, except that no approval by the electorate shall be required unless required by the State Constitution.

In the instant case, the City has determined to issue \$300,000,000 of revenue bonds for the stated purpose of investing the overwhelming portion of Bond proceeds in an investment contract, the principal of and interest on which will be pledged to owners of such Bonds. A proportionately miniscule amount of Bond proceeds, shown by testimony to be approximately \$1.5 million (App. 5, p. 15), is intended by the City to be applied to the "Project": park and recreational facilities, funding of self-insurance reserves or other municipal purposes. (App. 2, Exhibit 1, p. 3).

Appellant does not dispute that the undertakings proposed to be financed with the \$1.5 million dollars of profit are valid municipal functions or services. However, Appellant strongly contends that any analysis of whether bonds are issued in conformity with Article VIII, Section 2 of the Florida Constitution and Section 166.111, Florida Statutes (1985) for a municipal purpose must scrutinize the application of proceeds of the Bonds, not merely the use of investment earnings realized from such proceeds. An analysis of the application of proceeds of the City's proposed Bonds reveals that they are not applied toward any valid municipal

function or service, but merely to the acquisition of an investment for the City.

The use of bond proceeds in such a fashion appears to be a case of first impression in Florida, but it would seem clear that while cities may have valid governmental powers to make investments of available City moneys, the borrowing of moneys to invest should not be considered a municipal purpose.

The potential for abuse is manifest. A city could issue many hundred millions of dollars of bonds, direct some infinitesimal amount of earnings on bond proceeds to an acknowledged "municipal purpose," then apply the grossly disproportionate amount of bond proceeds to the acquisition of land, stocks, bonds or any investment for which the city can find a creditor (i.e., a bondholder) willing to accept the risk that such investment will be able to repay his loan. The borrowing of money primarily for the purpose of investment is not a recognized municipal function within the intendment of Article VIII, Section 2 of the Florida Constitution. The City thus having failed the first part of the two-part test for a valid exercise of home-rule powers, is not entitled to validation of its Bonds.

However, even if this Court takes exception to this part of Appellant's thesis, the City cannot comply with the second part of the valid exercise test because there exists superceding legislation in the form of Chapter 166, Part II, Florida Statutes (1985) prohibiting the contemplated bond issuance.

The description of the Bonds contained in Resolution 87-2 and the testimony presented by the City at the validation hearing characterizes them as "revenue bonds" to be repaid from revenues derived from sources other than ad valorem taxes on real or tangible personal property.

The Bonds clearly do not fit within the definitions of general obligation bonds, ad valorem bonds, improvement bonds or refunding bonds set forth in Section 166.101, Florida Statutes (1985), and indeed the City has titled them "Revenue Bonds".

The general authority for issuance of bonds contained in Section 166.111, previously cited, contains language permitting the pledge of "funds, credit, property and taxing power of the municipality for the payment of such debts and bonds." These provisions, however, may be further limited according to the type of bonds issued by other statutory provisions or the Florida Constitution. For example, the power to pledge ad valorem taxing power of a city to bondholders is limited by Article VII, Section 12 of the Florida Constitution governing local bonds, to bonds approved by vote of the electors.

Similarly, "revenue bonds" as defined in Section 166.101(4) are subject to the limitation that property, credit or general tax revenue of the municipality may not be pledged to the repayment of the bonds. The City, having elected to issue "revenue bonds," is subject to the statutory limitation imposed by Chapter 166, Part II and cannot pledge its property to the holders of such Bonds. The City intends to borrow money to acquire the contemplated

investment contract which will be pledged to the Bondholders. This transaction is no temporary pledge of security until bond proceeds are applied to a municipal purpose. The sole use of bond proceeds is this prohibited pledge of City property.

In keeping with the philosophy expressed in the Florida Constitution's broad home-rule powers granted to municipalities, the legislature has provided very liberal guidelines for municipal borrowing in Chapter 166, Part II. However, also in keeping with the mandate of Article VIII, Section 2 of the Florida Constitution, municipalities are not granted total unbridled power in their financial undertakings. In seeking to issue the Bonds for their stated purpose of investing the proceeds and pledging the investments to Bondholders the City has roamed beyond even the nearly borderless limits of home-rule powers. Accordingly, the Circuit Court judgment validating the Bonds should be reversed.

ISSUE II: THE COURT ERRED IN VALIDATING THE BONDS BECAUSE THE CITY HAS FAILED TO REQUIRE PROCEEDS OF THE BONDS TO BE INVESTED IN ACCORDANCE WITH SECTION 166.261, FLORIDA STATUTES (1985).

Municipal home-rule powers with respect to finance and taxation are addressed by general law in Chapter 166, Part III, Florida Statutes (1985). Specifically, Section 166.261, Florida Statutes (1985) requires that surplus public funds in the control or possession of a city must be invested in:

(a) The Local Government Surplus Funds Trust Fund;

(b) Negotiable direct obligations of, or obligations the principal and interest of which are unconditionally guaranteed by, the United States Government at the then prevailing market price for such securities;

(c) Interest-bearing time deposits or savings accounts in banks organized under the laws of the United States and doing business and situated in this state, in savings and loan associations which are under state supervision, or in federal savings and loan associations located in this state and organized under federal law and federal supervision, provided that any such deposits are secured by collateral as may be prescribed by law;

(d) Obligations of the federal farm credit banks; the Federal Home Loan Mortgage Corporation, including Federal Home Loan Mortgage Corporation participation certificates; or the Federal Home Loan Bank or its district banks or obligations guaranteed by the Government National Mortgage Association; or

(e) Obligations of the Federal National Mortgage Association, including Federal National Mortgage Association participation certificates and mortgage pass-through certificates guaranteed by the Federal National Mortgage Association.

Surplus funds are defined in Section 166.261(4), Florida Statutes (1985) to be:

(4) For the purposes of this section, the term "surplus funds" in any general or special account or fund of the municipality, held or controlled by the governing body of the municipality, which funds are not reasonably contemplated to be needed for the purposes intended within a reasonable time from the date of such investment.

Since the proceeds of the Bonds themselves will be invested and used to repay the Bonds over a period of up to ten years (App. 5, p. 18), the Bond proceeds arguably constitute "surplus funds" within the meaning of the cited Section 166.261(4). It follows then, that such funds are required to be invested in the investments outlined above. The investment contract described by the City's witness (App. 5, p. 15-16, 23-24) and permitted by Resolution 87-2 (App. 2, Exhibit 1, p. 2) and the Indenture (App. 2, Exhibit A to Exhibit 1, p. 3) does not fall within these definitions. Without the addition of a requirement in the Indenture that proceeds of the Bonds be invested in accordance with Section 166.261, Florida Statutes (1985), the Bonds should not have been validated.

CONCLUSION

As Appellant has shown, the application of approximately \$295,500,000 of proceeds of the City's \$300,000,000 of Bonds to acquisition of an investment contract to generate \$1.5 million of moneys for the City's municipal purposes does not constitute a permitted municipal function under Article VIII, Section 2 of the Florida Constitution, nor a legal issuance of revenue bonds under Section 166.101, Florida Statutes (1985). In addition, investment of Bond Proceeds in the described investment contract violates the requirements of Section 166.261(4), Florida Statutes (1985) governing investment of surplus public funds. Accordingly, the Final Judgment validating the City's Bonds should be reversed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by hand delivery to Elise F. Judelle, Bryant, Miller and Olive, P.A., 201 S. Monroe Street, Tallahassee, Florida 32301, this 16th day of March, 1987.



Alton O. Paulk
Assistant State Attorney