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January 27, 2021

## Bonds Issued Under Local Government Public Obligations Act of 1986

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We hope this information will be useful to you; reference to it will assist you with many of the questions that will arise in your tenure with county government. However, the *Tennessee Code Annotated* and other relevant laws or regulations should always be consulted before any action is taken based upon the contents of this document.

Please feel free to contact us if you have questions or comments regarding this information or any other e-Li material.

Sincerely,

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## Table of Contents

Bonds Issued Under Local Government Public Obligations Act of 1986 ...	3
General Obligation (G.O.) Bonds .....	3
Capital Outlay (C.O.) Notes .....	3
Bond Anticipation Notes .....	4
Revenue Bonds .....	4
Refunding Bonds - General Obligation and Revenue .....	4
Grant Anticipation Notes .....	4
Tax (Revenue) Anticipation Notes .....	4

## Bonds Issued Under Local Government Public Obligations Act of 1986

**Reference Number:** CTAS-1720

This act is codified in T.C.A. §§ 9-21-101 through 9-21-1017. Its purpose was to consolidate statutes pertaining to debt obligations of the county and to provide a uniform and comprehensive statutory framework authorizing any local government to issue long-term debt to fund costly capital improvement projects.

Authorized purposes for issuing notes and bonds are listed under T.C.A. § 9-21-105(20). Also, any local government may issue general obligation bonds under this act for certain unfunded pension obligations if approved by the state funding board after receiving a recommendation by the state director of local finance. T.C.A. § 9-21-127. The powers of local governments are described in T.C.A. § 9-21-107. All interest income received by investors buying notes or bonds issued under this act is generally exempt from federal income taxes, and by statute, exempt from all state, county, and municipal taxation except inheritance, transfer, and estate taxes. T.C.A. § 9-21-117. However, there are federal restrictions regarding earnings from borrowed funds, so it is important for counties to consult with a financial advisor regarding these arbitrage regulations.

All notes issued under this act must first be authorized by resolution adopted by the county legislative body and then approved by the state director of local finance, a division of the state comptroller of the treasury. Before the director of local finance will approve notes, the county must adopt a balanced budget, which must also be approved by this same director. T.C.A. §§ 9-21-403, 9-21-404.

The bonds and notes that can be issued under the Local Government Public Obligations Act are described on the pages below.

### General Obligation (G.O.) Bonds

**Reference Number:** CTAS-1716

G.O. bonds are usually issued for buildings and other major improvements when the life of the capital improvement will last longer than 12 years. Depending on the amount to be issued in a calendar year and current Internal Revenue Service regulations, the bonds may be exempt from federal income tax. The estimated rate of interest will be from four percent to six percent at the time of the writing of this publication. The rate will also depend on maturity of the issue and the credit rating of the issuer.

Upon the issuance of a general obligation (GO) bond, the county pledges the full faith, credit, and unlimited taxing power of the county as to all taxable property in the county or a designated portion of the county. T.C.A. § 9-21-201. These bonds may be issued with a maturity of up to 40 years; however, investors usually prefer 15 to 20 years. T.C.A. § 9-21-213(a). Counties are generally mandated to provide various services and are given the power to provide funding for these services, with certain restrictions. Under this act, registered voters may petition the county for an election on the issuance of the proposed bonds. T.C.A. § 9-21-207. Also, the county legislative body may hold a voluntary election. T.C.A. § 9-21-208. Refer to T.C.A. §§ 9-21-101 through 9-21-216 or T.C.A. §§ 49-3-1001 through 49-3-1007 for school bonds.

### Capital Outlay (C.O.) Notes

**Reference Number:** CTAS-1721

Capital outlay notes are used by local governments to fund many types of capital improvement projects. The notes may be issued initially for a period not to exceed the end of the third fiscal year following the fiscal year in which the notes were issued, then renewed for two more such periods not exceeding three years each with the approval of the state director of local finance. At least one-ninth of the original principal amount of these notes must be retired each year, unless this requirement is waived by the state director of local finance. T.C.A. § 9-21-604. Notes also may be issued for more than three but no longer than the 12th fiscal year following the fiscal year in which the notes were issued. T.C.A. § 9-21-608. Issues of 12-year notes totaling less than \$2 million may be sold at competitive sale or through the informal bid process described in the statute; notes totaling more than \$2 million must be sold by competitive sale.

T.C.A. § 9-21-608. A major advantage of issuing capital outlay notes is that the service of a fiscal advisor may not be needed. The notes are subject to the same restrictions as G.O. bonds for exemption from federal income taxes. These notes may be issued under T.C.A. §§ 9-21-601 through 9-21-610 depending on the maturity.

## Bond Anticipation Notes

**Reference Number:** CTAS-1722

If the market conditions are not favorable to issue G.O. bonds, a local government may issue bond anticipation notes not to exceed two two-year terms. These are obligations of the local government just like other bonds and notes; however, when the G.O. bonds are issued and the proceeds are received, these notes will be retired from the G.O. proceeds. These notes are subject to the same restrictions as G.O. bonds for exemption from federal income taxes. These notes are similar to construction loans in the business world. Using these notes allows the county time to wait for better interest rates or marketing conditions. These notes may be issued under T.C.A. §§ 9-21-501 through 9-21-505.

## Revenue Bonds

**Reference Number:** CTAS-1723

If the capital improvement is for income producing services, such as water and sewer, the local government should consider the issuance of revenue bonds. When revenue bonds are issued, the income or revenues from the project are pledged to secure the debt. The debt will be retired from revenues or income from the user charges. These bonds may be issued under T.C.A. §§ 9-21-301 through 9-21-316.

## Refunding Bonds - General Obligation and Revenue

**Reference Number:** CTAS-1724

When general obligation or revenue bonds are issued at high interest rates, they will have a callable feature allowing the county to recall the unpaid bonds or notes. In order to have funds to recall these bonds or notes, the county may issue refunding bonds. These bonds use the same pledge for security and replace the original issue with a lower rate of interest. By issuing the refunding bonds at a lower rate of interest, the county will save by paying less interest over the remaining term of the issue. T.C.A. §§ 9-21-901 through 9-21-1017.

## Grant Anticipation Notes

**Reference Number:** CTAS-1725

Whenever the county has a contract to receive a grant from the federal or state government, the county can issue grant anticipation notes of up to three years, or for longer specified periods with the approval of the state director of local finance, secured by the funds to be received under the grant. T.C.A. §§ 9-21-701 through 9-21-705.

## Tax (Revenue) Anticipation Notes

**Reference Number:** CTAS-1726

Whenever cash flow is not sufficient to meet current expenses, which usually occurs as a result of inadequate accumulated fund balances, the county may issue revenue anticipation notes, subject to the approval of the state director of local finance. An important point: These notes must be paid off by June 30th of the fiscal year in which they are issued. This requirement insures against the approval of a deficit budget. T.C.A. §§ 9-21-801 through 9-21-803.

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