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CITY AND COUNTY OF HONOLULU

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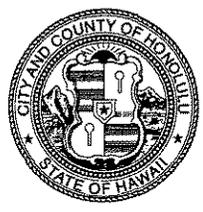
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CITY COUNCIL
HONOLULU, HAWAII



MUFI HANNEMANN
MAYOR

April 23, 2007

The Honorable Romy M. Cachola
Councilmember
City Council
Honolulu Hale
Honolulu, Hawaii 96813

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CITY CLERK
HONOLULU, HAWAII

Dear Councilmember Cachola:

Subject: Board of Water Supply Issuance of Revenue Bonds

This memorandum is issued in response to your inquiry dated April 2, 2007, presenting several questions regarding the issuance of revenue bonds by the Board of Water Supply ("BWS").¹ As discussed hereinbelow, we are of the position that BWS is empowered to issue BWS revenue bonds without the prior approval of the City Council.

A copy of your inquiry is attached. The specific questions presented are as follows:

1. Does BWS require Council approval to issue revenue bonds?
2. Is House Bill 259 (2007) intended to give favorable tax treatment to BWS on the interest of these bonds?

¹We requested from you and you authorized us to share with representatives of BWS the fact of your opinion request to COR to allow us to obtain information from BWS to prepare our response to your inquiry.

3. Does this power apply only to revenue bonds, or are other bonds included?

BACKGROUND

A. BWS Authority

Revised Charter of the City and County of Honolulu ("RCH") Section 7-105(h) provides that the Board of BWS² is empowered to issue revenue bonds in its own name, *i.e.*, under the name of the "board of water supply." RCH Section 7-113 pertaining to bond sales provides that when directed by the Board of BWS, the Director of Budget and Fiscal Services shall sell revenue bonds as may be authorized by the Board of BWS for the acquisition, construction, replacement, extension or completion of water systems in accordance with the procedures prescribed by law for such sales. Lastly, RCH Section 7-119 provides that aside from RCH Article VII, no other provisions of RCH shall apply to BWS.

We have searched the Council records and have identified four instances since 1994 when BWS has solicited and obtained Council authorization by resolution for the issuance of BWS revenue bonds. The resolution numbers for these authorizations are: 05-418, CD1; 03-202, 01-073 and 95-279. We understand that prior thereto, BWS requested issuance of general obligation bonds of the City and County of Honolulu and pursuant to the provisions of Hawaii Revised Statutes ("HRS") Chapter 47, prior approval of the City Council was solicited for the issuance of general obligation bonds of the City and County of Honolulu. The City Council is authorized under RCH Section 3-116.1 to issue general obligation bonds, and under HRS Section 47-6, prior approval of the City Council is required for issuance of general obligation bonds of the City and County of Honolulu. In contrast to revenue bonds, the full faith and

²RCH Section 7-102 clarifies in its definitions that here, the reference to BWS is to the board (and not the department) that is authorized to issue revenue bonds.

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credit of the City and County of Honolulu is pledged for the payment of the principal of and interest on general obligation bonds under HRS Section 47-12.

B. House Bill 259 (2007) Relating to Counties

A copy of House Bill 259 (2007) is attached. The Bill proposes amendments to HRS Section 49-3 pertaining to county revenue bonds, to specifically provide, among other amendments, that when authorized by a county charter to issue revenue bonds in its own name, a county board of water supply may exercise all of the powers vested in the county under Chapter 49 (for issuance of county revenue bonds) but only with respect to an undertaking or loan program under the jurisdiction of the county board of water supply.

HRS Chapter 49 also provides for the preferential tax treatment of revenue bonds issued under the Chapter. As to State or local taxes, HRS Section 49-14 states in part as follows:

Revenue bonds issued pursuant to this chapter and the income therefrom shall be exempt from all taxation by the State or any county or other political subdivision thereof, except inheritance, transfer, and estate taxes.

HRS Section 49-15 provides in part as follows as to federal tax exempt status:

Revenue bonds issued under this chapter, to the extent practicable, shall be issued so as to comply with requirements imposed by valid federal law providing that the interest on the bonds shall be excluded from gross income for federal income [tax] purposes (except as certain minimum taxes or environmental taxes may apply). The director of finance is authorized to enter into such agreements, establish such funds or accounts and take any action as required in order to

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comply with such valid federal law. Nothing in this chapter shall be deemed to prohibit the issuance of revenue bonds, the interest on which may be included in gross income for federal income tax purposes.

In the adopted minutes of the Council's Intergovernmental Affairs Committee meeting on February 28, 2007, the minutes report that Mr. Dean Nakano, Deputy Manager and Chief Engineer of BWS, appeared and presented oral testimony on Resolution No. 07-074 Relating to the Board of Water Supply. The adopted minutes report that Mr. Nakano noted that the intent of House Bill 259 was to deal with tax exemptions and not to circumvent the Council's authority. The minutes also report that Mr. Nakano confirmed that BWS would be requesting withdrawal of House Bill 259.

C. Hawaii Revised Statutes Chapter 49 Relating to Revenue Bonds

HRS Chapter 49 is the State authorization of authority to the counties and their boards of water supply to issue revenue bonds. HRS Section 49-1 sets forth definitions of terms applicable in HRS Chapter 49, the Section defines "county" to mean the City and County of Honolulu and the counties of Hawaii, Kauai and Maui, and the Board of Water Supply of the City and County of Honolulu and the Boards of Water Supply of the counties of Hawaii, Kauai and Maui; defines "board" to mean any department or board of any county authorized to issue revenue bonds under this Chapter; and defines "governing body" to mean the council of each county, "or any other body exercising the legislative powers of the county."

HRS Section 49-3, entitled, "Additional powers of counties," states in part as follows:

Subject to the approval of the governing body, a board may exercise all or any part of the powers vested in the county pursuant to this

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chapter but only with respect to an undertaking or loan program under the jurisdiction of such board. In the event a board shall exercise any of the powers vested in the county pursuant to this chapter, the term governing body as used in this chapter shall be deemed to mean the board, and the term director of finance shall be deemed to mean the chief financial officer of the board.

The authorization to issue revenue bonds is set forth in HRS Section 49-4, entitled, "Authorization of undertaking, loan program and revenue bonds; details of revenue bonds," and states in Section 49-4(a) as follows:

The acquisition, purchase, construction, reconstruction, improvement, betterment, or extension of any undertaking or the establishment and administration of a loan program may be authorized under this chapter, and revenue bonds may be authorized to be issued under this chapter by resolution or resolutions³ of the governing body of the county issuing the revenue bonds which may be adopted at the same meeting at which the same are introduced by a majority of all the members of the governing body of the county then in office and shall take effect immediately upon adoption.

DISCUSSION

A. Council Approval for Issuance of BWS Revenue Bonds

Your first inquiry asks whether Council approval is required for the issuance of revenue bonds by BWS. Based upon a plain reading of the language of HRS Sections 49-3

³We find it significant that the analogous provision addressing the authorization for issuance of general obligation bonds of the county in HRS Section 47-6, provides for authorization by ordinance as well as resolution by the legislative body of the county.

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and 49-4, we are of the opinion that BWS may issue revenue bonds for an undertaking or loan program under the jurisdiction of BWS and subject only to the approval of BWS. HRS Section 49-4(a) quoted above, empowers the "county" to issue revenue bonds with the authorization by resolution adopted by a majority of the members of the "governing body" of the "county." HRS Section 49-3, quoted in part above, provides that a "board" may exercise the powers vested in the "county" under HRS Chapter 49 for an undertaking or loan program under the jurisdiction of the "board," where the term "governing body" applicable to the county issuance of revenue bonds is deemed to mean the "board." We read these two provisions in conjunction with one another to authorize BWS to issue revenue bonds for an undertaking or loan program under the jurisdiction of BWS and subject only to the authorization by resolution adopted by a majority of the members of the Board of BWS.

B. House Bill 259 (2007) Intended for Favorable Tax Treatment

Your second inquiry asks whether House Bill 259 (2007) is intended to give favorable tax treatment to BWS on the interest of these bonds. Our understanding of BWS's proposal for House Bill 259 was to clarify whether City Council approval was required for issuance of BWS revenue bonds, to ensure that BWS's issuance of its revenue bonds was fully in accordance with the provisions of HRS Chapter 49 and to ensure that the BWS-issued revenue bonds would then be assured the favored tax treatment afforded to revenue bonds issued pursuant to HRS Chapter 49. In this context, we confirm then that House Bill 259 was intended to ensure the favored tax status of BWS-issued revenue bonds. The damage resulting from the loss of the anticipated favored tax treatment for a large bond issuance can reasonably be foreseen to be great and in the evaluation of BWS may not be a risk it determines it prudently can assume.

C. BWS Authority to Issue Bonds

We understand your last inquiry to assume that Council approval is not required for BWS issuance of BWS revenue bonds and asks whether this power to issue revenue bonds without Council approval applies only to revenue bonds or to other bonds as well. We confirm that BWS authorization to issue bonds without prior City Council approval applies only to revenue bonds issued in the name of BWS for an undertaking or loan program under the jurisdiction of BWS.

Under our Charter, RCH Section 7-105(h), BWS is authorized to issue only revenue bonds in its own name. Of the county bonds authorized in State statute, BWS is empowered only to issue revenue bonds based upon the Charter-described powers of BWS and the limitations set forth in the applicable State statutes authorizing county bonds.⁴ As mentioned, historically, BWS solicited the issuance of City and County of Honolulu general obligation bonds; however, such issuances are not BWS bonds but bonds of the City and County of Honolulu and prior Council approval is required for the issuance of county general obligation bonds. The procedure for BWS issuance of BWS revenue bonds set forth in HRS Chapter 49 that authorizes BWS to issue revenue bonds for an undertaking or loan program under the jurisdiction of BWS and subject only to the authorization by resolution adopted by a majority of the members of the Board of BWS, is unique to revenue bonds

⁴See, for example, HRS Chapter 48 that authorizes issuance of Economic Development Bonds by a political subdivision of the State to finance the purchase or lease of land, the purchase or construction of improvements, and the purchase and installation of equipment for use in connection with the development of an agricultural, industrial, commercial or hotel enterprise; and HRS Chapter 48E that authorizes a county to issue special purpose revenue bonds to finance pollution control projects, where a pollution control project is defined as a processing enterprise that is certified as necessary or desirable by the State Department of Health for the disposal of solid waste including facilities that provide for the recovery of energy or material resources.

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as BWS is not authorized to issue any other character of bond in its own name.

CONCLUSION

In response to your inquiry, we opine that BWS is authorized to issue revenue bonds for an undertaking or loan program under the jurisdiction of BWS and subject only to the authorization by resolution adopted by a majority of the members of the Board of BWS. Prior City Council approval is not required for the issuance of BWS revenue bonds. We defer to BWS's evaluation of the need for State statutory clarification of its bond authorization statute but fully appreciate that it may determine that the risk to its bond holders of the loss of a favored tax treatment is such that pursuing a clarifying State statutory amendment is warranted. BWS is not authorized to issue other bonds in its own name so the bond authorization procedure applicable to revenue bonds issued in BWS's name does not apply to other BWS issued bonds.

We are available to meet to discuss further or additional questions you may have on this matter.

Very truly yours,



DIANE T. KAWAUCHI
Deputy Corporation Counsel

APPROVED:



CARRIE K. S. OKINAGA
Corporation Counsel

DTK:ct
Attachs.