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Louisiana Beefs Up Statutory Lien in Rewrite of Local Bond Financing Law.

In a revamp of Louisiana's public financing laws, state legislators strengthened the statutory lien on local governmental bonds, a move prompted by high-profile municipal bankruptcies such as Detroit's.

Clarifying the lien wasn't the Legislature's primary goal in revising the state's bond laws, which was the result of a comprehensive effort to modernize and consolidate financing regulations, according to those who spearheaded it.

"The reorganization and new laws put into place will provide additional confidence to investors," said Sen. Eric LaFleur, D-Ville Platte. "It may mean savings to issuers in the form of lower rates."

LaFleur sponsored Senate Bill 426 – the Consolidated Local Government Public Finance Act – which lawmakers approved unanimously earlier this year and was signed into law by Gov. John Bel Edwards.

The new law was the result of a two-year project led by LaFleur, who consulted with a group of about 20 volunteer public finance officials across the state – bond attorneys, financial advisors and underwriters – who agreed to participate in a process LaFleur said was necessary to eliminate old rules and modernize the bond statute.

Among the many changes, the act clarifies that the statutory lien on bonds issued by local governments "shall be secured debt entitled to the highest possible protection and priority afforded by the bankruptcy laws of the United States and this state."

The old law said nothing about protection of the lien in bankruptcy.

"It wasn't clear how strong the lien was on the revenue stream that secured the debt," said LaFleur, a bond attorney and partner at Mahtook & LaFleur in Lafayette. "So we went in and clarified that."

LaFleur, 54, is also chairman of the Senate Finance Committee and a member of the State Bond Commission, which by law approves bonds issued by the state and local agencies. LaFleur says he recuses himself from voting when his clients appear before the commission.

Many of Louisiana's local municipal finance laws had been on the books since the early 1980s and needed to be updated or rewritten, according to LaFleur.

Some regulations were placed into various statutes in a piecemeal fashion, he said, while others required more clarification to provide uniformity in nomenclature and some needed to be deleted.

SB 426 became Act 569 in state law. It clarifies things such as when issuers can use bond resolutions or ordinances, deletes the requirement that issuers register sales tax bonds with the secretary of state, and provides for less ambiguity, LaFleur said.

The law also clarifies that school districts can issue all kinds of revenue bonds. The previous law was more narrowly interpreted.

The new law also clarifies the definitions of general obligation bonds, limited tax bonds, sales tax revenue bonds, and more.

“Deals are cleaner, and [easier] to understand,” LaFleur said.

This is not the first time LaFleur has tackled Louisiana municipal bond issues.

In 2014, he got SB 384 passed requiring that municipal securities issuers in Louisiana comply with the Securities and Exchange Commission’s Rule 15c2-12, as well as maintain a list of securities, continuing disclosure agreements, and current ratings.

SB 384 also requires that auditors make sure issuers are fulfilling recordkeeping duties, and that they review a sample of filings on the Municipal Securities Rulemaking Board’s EMMA filing system to determine if they comply with disclosure agreements.

If issuers don’t comply with the state’s disclosure requirements, they are “flagged” but not penalized.

The disclosure law is working, LaFleur said in an interview Tuesday. “Now [issuers] are regularly updating disclosures, at least that’s what I’m finding,” he said.

This year’s new bond law applies to traditional local governmental bonds.

It doesn’t apply to New Orleans because it operates under a charter, and it doesn’t apply to conduit issuers, 501(c)(3) tax-exempt nonprofit organizations, or exempt activity and multifamily bonds.

The new law says bondholders “have a statutory lien on and a security interest in such taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts as are pledged to the payment of such bonds,” and any pledge or grant of a lien or security interest shall be valid, binding, and perfected from the time when the pledge or grant of lien or security interest is made.

The lien will have first priority and will be binding as against all parties having claims of any kind in “tort, contract, bankruptcy, or otherwise against the governmental entity,” the law says.

Extreme diligence is warranted when investors consider whether a statutory lien exists, Municipal Market Analytics Managing Director Lisa Washburn wrote Monday in a comment about the financial struggles of Puerto Rico.

“There should be no optionality or action required for the lien to attach within the statute that is the basis for determining the existence of a statutory lien,” Washburn wrote in MMA’s Weekly Outlook. “If the language is unclear or leaves doubts, consultation with an experienced attorney may be needed.”

LaFleur said Louisiana’s original law on statutory liens was not clear or uniform, and that the law was rewritten in part because of Detroit’s Chapter 9 bankruptcy case.

Detroit exited bankruptcy in December 2014, shedding $7 billion of its $18 billion in debts, which included losses for holders of the city’s unlimited tax general obligation bonds.

Presiding U.S. Bankruptcy Judge Steven Rhodes questioned whether Michigan's law created a statutory lien on Detroit's ad valorem taxes because the statute didn't include the word "lien," according to a 2015 report by Breckinridge Capital Advisors on "The Changing Status of Statutory Liens."

Detroit defaulted on all its bond debt, highlighting the need for there to be precise statutory language regarding liens in order to benefit bondholders, the Breckinridge report said.

In Louisiana, the state's statutory lien law is now "more explicit than it was before" Act 569 was passed, said David M. Wolf, a bond attorney who worked with LaFleur on changes to the local public finance law.

Wolf said the old state law language on the lien was enacted in the early 1980s.

"I thought it would be better to write something that was written specifically with a bankruptcy case and a bankruptcy judge in mind," said Wolf, who is special counsel for Adams and Reese LLP based in the firm's New Orleans office. "There were uncertainties about the nature of bondholders' rights," he said.

"We were in a position of redrafting the law and one thing we wanted to do is think about changes in case law and practices," he said. "We also made sure that same kind of language would apply to all municipal bonds."

In Louisiana, cities and parishes can file for bankruptcy with the approval of the State Bond Commission and the governor.

Wolf said he was not aware of any municipal bankruptcies in Louisiana since he began practicing 36 years ago, but before that there may have been Depression-era Chapter 9 cases and some water district defaults on USDA loans.

The precise wording in Act 569 came about because of difficulties lawyers faced in places such as Michigan, he said.

"You never know when a bankruptcy is going to come about," Wolf said.

"Because in Louisiana almost all debt is secured by a specific stream of revenue, we now have a uniform place to go once it's decided what the source of security will be," he said. "You come to this statute."

One new feature of the financing law, he said, is the authorization that a limited revenue bond can be secured by parcel fees or service charges. Fire departments, for example, can leverage a fee charged for fire services.

"We just tried to make [the new law] consistent with the way the markets and regulations have evolved the last 30-40 years," he said. "We consolidated, modernized and streamlined. I hope it's an approach other states adopt."

LaFleur said the state has been proactive about updating bond laws, and he expects some tweaks to Act 569 to be made during next year's legislative session.

The new public financing act will make it easier for bondholders to understand Louisiana's laws, said LaFleur, who believes the State Bond Commission will consider approving local bond issues under the law as early as the panel's meeting on Thursday.

“I’m hoping someone out there will say Louisiana is trying to be progressive,” he said.

The Bond Buyer

By Shelly Sigo

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