Bonds—Funding Bonds—Exchange of Funding Bonds for Outstanding Warrants—Validity of Funding Bonds Exchanged for Outstanding Warrants Without Submitting the Issuance of Same to a Vote of Electors When the Same Exceeds $10,000 in Amount.

Funding Bonds may be issued and exchanged for outstanding county warrants even though the same exceed $10,000 in amount, without submitting the proposition to the vote of the qualified electors of the county.

June 10th, 1918.

Mr. John F. McKay,
Co. Clerk and Recorder,
Thompson Falls, Montana.

Dear Sir:

I am in receipt of your letter of June 7th, 1918, relative to arrangement made with Ferris & Hardgrove of Spokane, for exchange of $75,000 outstanding road, bridge, and general fund warrants for a like amount of bonds, and requesting my opinion as to whether such exchange can be made without submitting the question to a vote of the electors of the county.

As I understand the proposition of Ferris & Hardgrove, they propose to buy up outstanding road, bridge and general fund warrants which, with accrued interest, will amount to $75,000.00, and then to exchange them for funding bonds issued by the county for the purpose of funding this warrant indebtedness. The funding bonds will not be sold, the cash received therefor being paid into the county treasury and used to pay the warrants and interest, but the funding bonds will simply be exchanged for the warrants.

In the case of Edwards vs. Lewis and Clark County, 53 Mont. 359, 165 Pac. 297, the county had sold the funding bonds, received the cash from the purchaser, and then called in the outstanding warrants and paid them with the cash received from the sale of the funding bonds, and the court held that selling the bonds and receiving the

cash therefor constituted a borrowing of money. Here the situation will be entirely different, as there will be merely an exchange of the evidence of the debt and the county will not receive or pay out any money.

In the case of Board of County Commissioners of Marion County vs. Board of County Commissioners of Harvey County, 26 Kan. 181-201, involving the validity of certain refunding bonds which had been issued, Mr. Justice Brewer, in delivering the opinion, said:

> "The funding amounts to this and nothing more: in lieu of one certain evidence of debt another is issued. In consideration, it is true, of a change in the time and interest, a change was made in the amount promised to be paid. But this change was a reduction, and therefore a benefit to the debtor. Still, neither the one paper nor the other was the debt itself, but only the written evidence thereof. The debt remains the same. The change was in the evidence of the debt. Notwithstanding the financial theories popular with a few, the law does not recognize a substitution of one promise to pay for another as in fact a payment, and looks evermore beyond the form of the transaction to the substance thereof, and, until the debt is in fact paid it calls it, in fact, the same debt, notwithstanding many changes may be made in the evidence thereof. The books are full of cases in which, after a note and mortgage have been once executed, the note has been again and again renewed and still the mortgage held as security for the debt with all its original priorities. (Pratt vs. Topeka, 12 Kan. 572.) Nor does it make any difference that changes are made in the rate of interest, time of payment, or in minor details, as long as the principal debt remains in fact unpaid."

In the case of Gelpcke vs. Dubuque, 1 Wall. (U. S.) 175, cited with approval in 1 Dillon Mun. Corp. Sec. 293, it was said:

> "A contract whereby a city agrees with an individual that if the latter will pay or advance the amount of interest due and to become due on certain bonds of the city already issued the city will pay or refund the amount is 'not a borrowing of money' within the terms and spirit of the charter prohibiting the municipal authorities from borrowing money unless authorized by a vote of the citizens, such a contract being one simply for the payment of a debt."

In the case of Opinion of Judges in re Bonds, (Me.) 18 Atl. 291, the Court said:

> "If the new bonds be exchanged for the old, bond for bond, it would literally be a renewal and extension of the debt * * *. The old bonds were evidence of the war debt. The new bonds become such evidence by substitution."

In the case of Board of Co. Commissioners vs. Society for Savings, 90 Fed. 233, the court said with reference to refunding bonds:

> "The refunding of a debt in the legal method prescribed in Doon Tp. v. Cummins, 142 U. S. 366-378, 12 Sup. Ct. 220,

is not borrowing money, nor is the exchange of bonds for a judgment the making of a loan. * * * *. Such an exchange neither creates nor increases the debt, it simply changes the form of it. The creditor loans no money and the debtor obtains none. * * * *. Chapter 50 of the laws of 1879 gave the board of county commissioners ample authority to refund debts evidenced by a judgment, without a vote of the electors of a county."

Colorado has a statute which authorizes a board of county commissioners to issue bonds in payment of judgments, no provisions being made for submitting the question of such refunding to the electors of the county. This statute was twice before the federal court. In the first case it was said:

"If the Parks judgment against the board of county commissioners of Lake County on April 16, 1891, evidenced a valid indebtedness of that county, the issue of the bonds, from which the coupons in suit were out, in payment of that judgment was not the creation of a debt and did not fall under the ban of the constitution. It was but an extension of the time for payment of a debt already existing and due, pursuant to plenary authority given to the board of county commissioners by the legislature of Colorado."

Board of Co. Commissioners vs. Pratt, 79 Fed. 567. (CCA 8th Cir.)

In the second case it was said:

"The answer to the proposition is that the prohibition of the constitution of Colorado is against the creation of a debt by loan, and the mere exchange of judgments against the county for its refunding bonds creates no debt by loan or in any other way. The debts exist before as well as after the exchange. The judgments and the bonds are nothing but the legal evidence of the existence of these debts and the exchange of the one for the other merely changes the form of the obligation."

Geer vs. Bd. Co. Comm. 97 Fed. 435. (CCA 8th Cir.)

In the case of McCreight vs. Zemp, (S. C.) 26 S. E. 984, it was said:

"This debt, in the case at bar, having already been legally contracted by the City of Camden, and it only needing the grant of power from the legislature to change the form of that legally contracted debt by placing it in bonds instead of an account, we see no reason why this matter should be held to have fallen under Section 23 of the act amending the charter of Camden."

In the case of City of Poughkeepsie vs. Quintard (N. Y.) 32 N. E. 764, the city had incurred a bonded debt for a water supply, and for the purpose of refunding such bonds, sold refunding bonds, intending to apply the proceeds derived from such sale to the payment of the old bonds. The purchaser of the refunding bonds refused to take

the new bonds upon the ground that it was a borrowing of money prohibited by the charter. In the course of the opinion the court said:

> "The transaction is in no way different from what it would have been had there been an exchange of bonds. There it is conceded there would have been no borrowing of money and merely an extension of credit. But the actual result and the contemplated purpose are exactly the same under the second form of refunding as under the first, and I do not think the permission of the enabling act comes within the prohibition of the charter. That prohibition has an obvious purpose and meaning. It was to restrict the creation of a debt and not the extension of one already existing; to prevent a new liability, and not to postpone payment of an old one; to shield the taxpayers from the waste and danger of extravagance and needless appropriations, and not to obstruct the convenient and beneficial extension of a proper debt lawfully created. * * * What may seem payment in form is not so in truth but a mode of substituting extended bonds for those matured taking the form of payment solely to compel the substitution intended."

This particular question was involved in and decided in the case of Hyde vs. Ewert (S. D.) 91 N. W. 474. The city charter of the City of Pierre, granting power to the city council, contained the following provision:

> "To borrow money on the credit of the corporation for corporate purposes, and issue bonds therefore, in such amounts and on such conditions as it shall prescribe; * * * provided no bonds shall be issued by the said city council under the provisions of this act, either for general or special purposes, unless, at an election, the legal voters of said city by a majority shall be determined in favor of said bonds," etc.

The City of Pierre was indebted in a large amount, evidenced by outstanding bonds and funding bonds. The city council, by the adoption of an ordinance, without submitting the question to the legal voters of the city, determined to refund a portion of such outstanding bonded indebtedness by issuing refunding bonds, and exchanging such refunding bonds for the outstanding bonds to the amount of the refunding bonds authorized by the ordinance.

The validity of such refunding bonds was attacked, it being contended, among other things, that they were invalid for the reason that the question of issuing said refunding bonds had not been submitted to and authorized by a majority of the legal electors at an election held for such purpose.

The court, however, decided adversely to such contention, holding that issuing refunding bonds and exchanging them for outstanding bonds was neither the borrowing of money nor the creation of a debt, but merely the substituting of one evidence of indebtedness for another, and that said act did not require the question of issuing such refunding bonds to be submitted to and authorized by a majority of the voters of the city.

Sections 2905 to 2908, inclusive, Revised Codes 1907, provide for the issuance of refunding bonds. Section 2907 provides for the sale of such bonds. Section 2908 provides that the proceeds derived from such sale must be paid into the county treasury, and must be applied to the payment of the bonds, warrants, or orders to be refunded. This section further provides that the board of county commissioners, instead of selling the bonds may exchange them for county warrants and orders which have been issued. This is direct authority to exchange such bonds for outstanding warrants, instead of selling the bonds and applying the proceeds in payment of the warrants.

I am of the opinion that when a county issues refunding bonds and exchanges them for outstanding warrants, instead of selling such bonds and applying the proceeds of such sale in payment of the outstanding warrants, the county neither borrows money nor creates a debt; that it is not necessary to submit to the electors of the county the question of issuing refunding bonds to be exchanged for outstanding warrants, before a county is authorized to issue and exchange such refunding bonds; and that the case of Edwards vs. Lewis and Clark County, supra, has no application to such question, but only implies when the bonds are to be sold and the proceeds of the sale are to be paid into the treasury and applied in payment of outstanding warrants.

Respectfully,

S. C. FORD,

Attorney General.