

COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT

ANTHONY GALLIS,	:	
WILLIAM BOTT, and	:	
ROBERT WILTSHIRE,	:	
	:	
Complainants,	:	Number: LGUDA-90
	:	LGUDA-93
v.	:	
	:	
DICKSON CITY BOROUGH,	:	
FRED JOSEPH, PAUL KWEIC,	:	
BARBARA MECCA, and	:	
REGINALD WROBEL,	:	
	:	
Respondents.	:	

OPINION AND ORDER

Statutory Background

The Local Government Unit Debt Act, Part VII of Act 177 of 1996, P.L. 1158, as amended, 53 Pa.C.S. §§ 8001 - 8271 (the "Debt Act" or "LGUDA"), governs the issuance of debt by local governments. The Debt Act is administered by the Department of Community and Economic Development (the "Department"). The Debt Act establishes procedures for the issuance of various kinds of debt, including general obligation non-electoral debt and "lease rental" debt, which pledges the full faith and credit of the local government unit in guaranty of another entity's borrowing. § 8002(a). Certain non-electoral borrowing for aggregate

amounts of less than \$125,000 may be issued by the local government unit without prior Department approval; however, notes improperly issued as small borrowings may be declared invalid by the Department. §§ 8109, 8208.

Taxpayers may contest the validity of the local government unit's actions related to debt issues by filing a complaint with the Department. § 8211(b). The Department has exclusive, but limited, authority to review actions by local government units, including:

exclusive jurisdiction to hear and determine all procedural and substantive matters arising from the proceedings of a local government unit . . . including the regularity of the proceedings, the validity of the . . . obligations of the local government unit and the legality of the purpose for which the obligations are to be issued.

53 Pa.C.S. § 8211(d); see also Bundy v. Belin, 501 Pa. 254, 461 A.2d 197 (1983). As such, the Department reviews the debt proceedings of local government units to ensure that the proceedings do not violate the Pennsylvania Constitution or the Debt Act. §§ 8111, 8204. The Department may also review and declare invalid debt instruments that are issued without compliance with the Debt Act. § 8208.

When a complaint under the Debt Act is filed with the Department, it is assigned to a presiding officer who has been appointed by the Secretary to fulfill that role. 12 Pa. Code § 11.14. The presiding officer administers the case and makes a report containing proposed findings of fact and conclusions of law to the Department's Secretary for the ultimate disposition of the matter. Id. Under the Department's regulations, a hearing or oral argument may be convened with respect to motions and complaints if and as necessary. See 12 Pa. Code §§ 11.11(c), 11.12(a).

There are two matters currently pending before the Department. In the matter docketed at LGUDA-90, the presiding officer reviewed the Complaint, the Borough's answer thereto, the Complainants' reply, and the Borough's letter of objection to the reply. In the matter docketed at LGUDA-93, the presiding officer reviewed the complaint and the debt proceedings submitted by the Borough to the Department. Based on these reviews, the presiding officer made the required recommendations for disposition of the two matters, which are, thus, ripe for disposition.

Background

LGUDA-90: On January 17, 2003, the Department received a complaint (the "Loan Complaint") filed by Anthony Gallis, William Bott and Robert Wiltshire (the "Complainants") and docketed at LGUDA-90. The Loan Complaint alleged that Dickson City Borough (the "Borough") had established a line of credit in the principal amount of \$300,000 (the "Loan") without Department review under the Debt Act. On February 5, 2003, the Borough filed an answer to the Complaint (the "Answer"). Within the seven-day period permitted by Debt Act regulations, by letter dated February 12, 2003, Complainants filed additional materials (the "Reply") responding to the Borough's Answer. See 12 Pa. Code § 11.9(b). The Borough objected (the "Objection") to the Reply by letter dated March 13, 2003, although, in the same letter, the Borough provided additional information of its own regarding the then-current balance of the Loan.

LGUDA-93: On March 26, 2003, the Complainants filed another complaint with the Department (the "Bond Complaint"), challenging an expected debt filing by the Borough. The Bond Complaint was docketed at LGUDA-93. On March 27, 2003, the Borough filed its proceedings (the "Debt Proceedings") with the Department, seeking approval of the Borough's proposed guaranty of up to \$7,900,000 of bond financing to be issued by the

Dickson City Golf and Recreation Authority (the "Authority"). The Borough's response to the Bond Complaint was received by the Department on April 29, 2003, more than a week late, and consisted primarily of ad hominem attacks on the Complainants. Pursuant to the Debt Act regulations, the Borough is "deemed in default, and the relevant basic facts, but no conclusions of law, stated in the complaint or petition shall be deemed admitted." 12 Pa. Code § 11.9(a)(1). As such, resolution of the Bond Complaint will be determined on the basis of the contents of the Bond Complaint and the Borough's Debt Proceedings.

Legal Standards

The General Assembly has provided a limited scope of review to the Department with respect to filings under the Debt Act, permitting the Department to determine only "(1) the regularity of the proceedings, (2) the validity of the bonds, and (3) the legality of the purpose for which the bonds are issued." Bethel Park Citizens for Better Educ. Less Taxes (BELT) v. Dep't of Cmty. Affairs, 563 A.2d 969 (Pa. Cmwlth. 1989) (citations omitted); 53 Pa.C.S.A. § 8211(d).

Under the Department's regulations, a complaint shall be dismissed

if the pleadings, together with affidavits or documents, if any, and the proceedings of the local government unit which are the subject of the complaint or petition show that there is no genuine issue as to a material fact and the moving party is entitled to dismissal of the complaint or petition as a matter of law.

12 Pa. Code § 11.11(b)(3).

Findings of Fact

The Department makes the following findings of fact, based on the respective pleadings and exhibits submitted to the Department:

1. The Borough established a \$300,000 line of credit with PennStar Bank on December 4, 2002. Answer, ¶ III.
2. The Borough made a draw on the line of credit in December in the amount of \$140,000. Loan Complaint, Exhibit 10; Answer, ¶ III.
3. The Borough did not at any time submit debt proceedings to the Department or receive approval of debt proceedings from the Department related to the line of credit.
4. On March 15, 2003, the Borough advertised in the Scranton Times, a newspaper of general circulation, that Borough Council would "consider the enactment of an ordinance . . . authorizing . . . the incurrence of lease rental debt of the Borough" The advertisement included a summary of the ordinance to be considered, and provided information as to where and when a full copy of the ordinance could be reviewed. Bond Complaint, Exhibit 1; Debt Proceedings, attachment (b).

5. On March 18, 2003, the Borough Council enacted an ordinance authorizing "the incurrence of lease rental debt by the Borough, in the maximum aggregate principal amount of seven million nine hundred thousand dollars (\$7,900,000)" Debt Proceedings, attachment (d); Bond Complaint, Exhibit 2 (Proposed Agenda of March 18, 2003 meeting).
6. The aggregate principal amount of the Borough's proposed lease rental debt will not exceed \$7,900,000. Debt Proceedings, attachment (f) (Debt Statement), at 2.
7. The Borough's Debt Statement does not reflect its \$300,000 Loan with PennStar Bank. Id.

Discussion

Complainants, who are members of the Dickson City Borough Council, have, in recent months, filed three separate complaints against the Borough and their four fellow members of Council, each complaint alleging some improper action by Council with respect to public financing issues within the jurisdiction of the Debt Act. LGUDA-90 alleges that the Borough established and

used its \$300,000 Loan with PennStar Bank without approval from the Department. LGUDA-92, which challenged the Borough's issue of tax anticipation notes, was not timely filed and was, thus, dismissed by the Department. LGUDA-93 alleges that the Borough has applied for approval of lease rental debt in excess of its calculated debt limit, and that insufficient notice was provided regarding the debt ordinance.

LGUDA-90

Complainants correctly assert that the Borough's \$300,000 Loan exceeds the limit for small borrowing for capital projects set forth in section 8109 of the Debt Act. Loan Complaint, ¶ III. Section 8109 permits a local government unit to incur debt without Department approval if "[t]he aggregate amount of the debt outstanding at any one time shall not exceed . . . \$125,000" § 8109(a)(1). The Loan from PennStar Bank, although established as a line of credit permitting draws of various amounts, provides the Borough with a credit facility that at any time could reach \$300,000. In its Answer, the Borough admits that the line of credit was established, but suggests that its intent was to never draw down more than \$124,999. Answer, ¶ III. Yet, within the first month the Loan was open, a draw was

made for \$140,000, placing the balance of the Loan above the Debt Act's limit. Id. If the Borough determined that it needed the flexibility of a \$300,000 credit facility, its wisest course of action would have been to pass an ordinance to incur that level of debt and submit appropriate debt proceedings to the Department for approval. By failing to do so, the Borough now finds itself with an invalid debt obligation.¹

In its Objection to Complainants' Reply, the Borough asserts that the outstanding balance of the Loan was reduced in February to approximately \$82,000. Objection at 1. This is, in effect, an admission by the Borough that the Loan balance remained above the section 8109 limit for two months. Regardless of the Borough's initial intent, both the practical limit and the practice of use of the Loan exceed the Debt Act's \$125,000 cap for small borrowing. The Loan is, thus, invalid. See § 8208(a).

Invalid debt instruments held by bona fide holders may be considered valid and enforceable if the holder was without actual knowledge of the lack of Department approval. See § 8208(b). PennStar Bank, however, cannot be considered a bona

¹The Borough states in its Answer that "a filing was made with DCED, under the 'small borrowing procedures' provided for in the Local Government

bona fide holder. The bank's commitment letter for the Loan sought "[e]vidence that bond proceedings have been filed with the Pennsylvania Department of Community and Economic Development" prior to closing. Loan Complaint, Exhibit 6, ¶ 8. There was no such filing with the Department. The bank closed the Loan without evidence of a Department filing, thereby waiving its own requirements and proceeding at its own peril. The bank, therefore, cannot be considered a bona fide holder of the Loan note, and the Loan remains invalid with respect to the bank.

Section 8208 further provides that the "local government unit may recover all interest and principal or other amounts payable thereon from the . . . individuals, including the officers of the local government unit, responsible for making the unapproved or unauthorized delivery." § 8208(c). These provisions are generally more applicable to instances where a local government unit has issued bonds or other debt that produce costs or penalties associated with the declaration that they are invalid, although some costs of refinancing or redeeming the Loan could be envisioned here.

The Loan Complaint raises meritorious issues regarding the Borough's line of credit with PennStar Bank, and, is, therefore,

Unit Debt Act." Answer, ¶ III. Department records show no such filing; moreover, the Debt Act does not have a procedure for small borrowing filings.

upheld. The Debt Act does not expressly define remedies for this situation. Presuming that the Borough does not wish to abandon the Loan entirely, and that the bank is willing to adjust its credit facility accordingly, the Borough appears to have two options: either reduce the upper limit of the Loan to \$125,000, or file appropriate debt proceedings with the Department to obtain approval to borrow up to the Loan's \$300,000 limit.

LGUDA-93

The Bond Complaint alleges that the Debt Proceedings filed by the Borough (i) attempt to increase its debt above its legally permitted calculated debt limit and (ii) provided insufficient notice of Council's plan to consider the ordinance incurring the lease rental debt. Bond Complaint, ¶ III. Both allegations are without merit.

Limits on incurring non-electoral or lease rental debt are calculated based on the "aggregate net principal amount of the new debt." § 8022(a), (b) (emphasis added). In preparing its debt statement, the Borough included the aggregate net principal balance of the \$7,900,000 in bonds to be issued by the Dickson City Golf and Recreation Authority, which the Borough's Debt

Proceedings seek to guaranty. See Debt Proceedings, attachment (f) (Debt Statement). Rather than using the principal amount of the bonds, Complainants relied on the total of principal and interest to be repaid. Bond Complaint, Exhibit 3. With the exception of omitting the Borough's Loan with PennStar Bank, the Borough's debt statement is correctly calculated and the new lease rental debt will not carry the Borough over its debt limit.

The Debt Act "provides an exclusive and uniform system" by which local government units "may borrow money on notes or bonds." § 8001(d). "Notwithstanding any other statute to the contrary, an ordinance required to be adopted by [the Debt Act] shall be advertised not less than three nor more than 30 days prior to its enactment." § 8003. The Borough advertised its ordinance on March 15, 2003 and adopted the lease rental debt ordinance three days later on March 18, 2003. Bond Complaint, ¶ III; Debt Proceedings, attachments (b), (d). Complainants argue that the notice was insufficient under the Borough Code; however, the Debt Act is the exclusive and controlling statutory authority when a local government unit wishes to borrow money. §§ 8001(d), 8003. The Borough, therefore, provided sufficient notice to meet the requirements of the Debt Act.

The Borough used the correct figures in its debt statement and followed Debt Act procedure to advertise its debt ordinance. Both of Complainants' allegations in the Bond Complaint are without merit and the Bond Complaint, LGUDA-93, is dismissed in its entirety.

Conclusions of Law

The Department determines the following conclusions of law:

1. As soon as the Borough made a draw from its Loan of more than \$125,000, the Borough incurred debt that required prior approval from the Department. The Loan is, therefore, invalid.
2. The Borough's Debt Statement correctly reflects the amount of lease rental debt for which it seeks approval, but should also include the amount of the Borough's Loan with PennStar Bank.
3. The Borough's notice of its consideration of an ordinance to incur lease rental debt was sufficient to meet the requirements of the Debt Act.

Conclusion

The Loan Complaint, LGUDA-90, raises legitimate issues that the Borough's Loan was improperly drawn without prior approval by the Department. The Loan is, thus, invalid. The Bond Complaint, LGUDA-93 is, however, without merit, and is dismissed in its entirety. The Debt Proceedings will be administratively processed by the Department as required by the Debt Act.

Dated this 15th day of May, 2003.

Dennis Yablonsky
Secretary of
Community and Economic
Development

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DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT

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ORDER

AND NOW, this 15th day of May, 2003, on review of the respective pleadings, papers, and exhibits in the matters before the Department docketed at LGUDA-90 and LGUDA-93, and on review of applicable law, **IT IS ORDERED** that the Commonwealth of Pennsylvania, Department of Community and Economic Development, pursuant to the Local Government Unit Debt Act, 53 Pa.C.S. §§ 8001 - 8271, declares Dickson City Borough's line of credit an invalid debt instrument, and **IT IS FURTHER ORDERED** that the Complaint at LGUDA-93 is dismissed in its entirety and the Debt Proceedings shall proceed for appropriate review by the Department.

Dennis Yablonsky
Secretary of Community and
Economic Development

Order Issued: May 15, 2003