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SYLLABUS:

1. The legislative authority of a village has the power to recognize as a moral obligation of the village interest payments and payments on principal received by the village on the credit of private individuals.

2. Such payments may be made directly to the lending institution.

3. The village may not, however, satisfy this moral obligation from the proceeds of general obligation bonds issued under Section 133.24, Revised Code, or mortgage revenue bonds issued under Section 12, Article XVIII, of the Ohio Constitution, for the purpose of acquiring, constructing, extending or operating a sewer system even though the moral obligation arose from a transaction in connection with the construction of the sewer system.

Columbus, Ohio, June 28, 1963

Hon. Roger W. Tracy
Auditor of State
State House
Columbus, Ohio

Dear Sir:

I am in receipt of your request for my opinion which is in substance:

“Briefly summarized, in 1960 a group of eight individuals (including the individual then serving as village mayor, the president of the board of public affairs; and

an engineer then under contract with the village for completion of a sewer system) borrowed money from a bank and deposited the proceeds of the loan in the village treasury to the credit of the Sewer Construction Fund.

“The borrowers gave a note to the lending bank, signed in their individual capacities. At the time of the alleged loan to the village, the private lenders appear to have received no official evidence of indebtedness of the village. There appears to have been no official act of the council with reference, either to receipt of the money or obligation of the municipality, as required by Chapter 133 of the Revised Code.

“The note given to the bank bears only the signatures of the individual borrowers and does not purport to bind the municipal corporation. The principal amount of the note remains unpaid, but the village has made periodic interest payments to the bank during the period of our examination. These payments were purportedly authorized by official action of the board of public affairs. Three of such payments were disbursed from the fund which was credited with the amount of the loan at the time of the initial payment into the treasury. A fourth disbursement for interest payment was made from the General Bond Retirement Fund of the village.

“Sometime subsequent to the date of the alleged receipt of the above amount bonds were issued and sold and the proceeds used for the purpose which was purportedly anticipated by the private lenders. No part of the alleged loan was satisfied out of the proceeds of the bond issue.

“Thereafter the village council passed an ordinance purporting to recognize an obligation of the village to satisfy the face amount of the note, together with all interest which has been paid or accrued under the personal and private obligation described above.”

Upon this factual situation you have propounded these basic questions:

1. Can the village recognize as a moral obligation the payment of principal and interest by these individuals.
2. Can payment under theory of moral obligation be paid by the village directly to the lending institution.
3. Can the village issue either general obligation or mortgage revenue bonds to obtain money for the satisfaction of this obligation.

At the outset, although probably unnecessary, it should be

stated that the village in question is a municipal corporation.

The first question, if unanswered before, is disposed of by *The State, ex rel. Caton v. Anderson*, 159 Ohio St., 159, in which it was held as disclosed by the first and second branches of the syllabus:

“1. A municipality has the authority to enact an ordinance appropriating money to pay a claim which is by law unenforceable against it but which on principles of justice and equity constitutes a moral obligation of the municipality.

“2. An obligation may be recognized by a municipality, where such obligation would be enforceable at law were it not for some rule which exempts the municipality in the particular instance from legal liability, or where the obligation is legally unenforceable but is binding upon the municipality in conscience and according to natural justice.”

There can be little doubt that the \$12,000.00 advance, upon the credit of private individuals, to the sewer construction fund of the village “on principles of justice and equity constitutes a moral obligation” of the village. If my conviction is not shared, I point out that the question is one primarily for the determination of the legislative authority of the village. *The State, ex rel. Caton v. Anderson, supra*.

I am likewise of the opinion that the moral obligation extends to interest payments as well as the payment of principal.

Nor am I able to see why this moral obligation may not be satisfied by payments directly to the lending institution. There would seem to be no reason, either legally or practically, why the village should be required to wait until payments of interest and repayments of principal have been made by the private persons who have loaned their credit to the village. The money was received (and presumably used) by the village and the moral obligation arose as of that time.

I will state here that it is my understanding that none of these private borrowers are presently members of the legislative authority or of any board or an officer or commissioner of the village.

The question remains whether the village may issue general

obligation or mortgage revenue bonds to obtain funds for the satisfaction of this moral obligation. Upon logical disquisition I think it becomes clear the village may not issue general obligation bonds to pay this moral obligation.

The issuance of general obligation bonds under authority of Section 133.24, Revised Code, is restricted to purposes of acquiring or constructing (including improving, extending and enlarging) a permanent improvement. In the instant case, while the circumstance giving rise to the moral obligation occurred in connection with the construction of a sewer system, the payment of the obligation itself is not necessary to the construction of the sewer system and can not be considered as a direct cost of acquiring or constructing this permanent improvement.

In Opinion No. 701, Opinions of the Attorney General for 1949, it was held, in response to a question similar on principle to the question here, in the first branch of the syllabus that:

“No part of the proceeds from the sale of general obligation bonds of a municipality may be used to pay the necessary incidental expenses, such as legal advertising, printing financial statements, notes and bonds, attorney fees for preparation of legislation and transcript of proceedings or opinion of bond attorney as to the legality of the bonds, incurred in the issuance of such bonds.”

The then Attorney General reasoned, page 359, that: “There appears to be no inference in any of the sections relating to the issuance of general obligation bonds by a municipality nor in the Uniform Bond Act from which incidental expenses of the proceedings to issue such bonds may be considered part of the cost of the improvement.”

The reasoning and conclusion of the 1949 Opinion were concurred in Opinion No. 788, Opinions of the Attorney General for 1951 wherein it was held in the third branch of the syllabus:

“A municipality is without authority to use any part of the proceeds from the sale of bonds issued in anticipation of the collection of special assessments, in payment of services of a firm or individual in promoting the sale of such bonds.”

It was also concluded, however:

“A municipality issuing mortgage revenue bonds pursuant to the authority of Section 12, of Article XVIII of the Ohio Constitution may if it deems it necessary to the most advantageous sale thereof, use a portion of the proceeds of such bonds in payment of a commission for their sale or for procuring and approving legal opinion of a reputable firm of bond attorneys as to the validity of such bonds.”

Which leads to the last question whether in the case under consideration the proceeds from an issue of mortgage revenue bonds could be used to satisfy this moral obligation.

The power of a municipal corporation to issue mortgage revenue bonds is derived not from statute but from Section 12, Article XVIII of the Constitution of Ohio, which provides:

“Any municipality which acquires, constructs or extends any public utility and desires to raise money for such purposes may issue mortgage bonds therefor beyond the general limit of bonded indebtedness prescribed by law; provided that such mortgage bonds issued beyond the general limit of bonded indebtedness prescribed by law shall not impose any liability upon such municipality but shall be secured only upon the property and revenues of such public utility, including a franchise stating the terms upon which, in case of foreclosure, the purchaser may operate the same, which franchise shall in no case extend for a longer period than twenty years from the date of the sale of such utility and franchise on foreclosure.”

It has been determined that Section 12, Article XVIII, is self-executing and self-sufficient, and utility mortgage bonds created and issued strictly within its terms are not affected by other parts of the Constitution or by the Uniform Bond Act. *Middletown v. City Comm.*, 138 Ohio St. 596.

It has also been held that a municipal corporation acts in a proprietary capacity in the ownership and operation of an utility under authority of Section 4, Article XVIII, of the Constitution, and may exercise its powers as an individual owner would. *Akron v. P.U.C.*, 149 Ohio St., 349. Further, that in owning and operating an utility, a municipality is free from statutory restriction or limitation. *State, ex. rel. McCann v. City of Defiance*, 167 Ohio St., 313; *Swank v. Shiloh*, 166 Ohio St., 415.

From this decisional authority it was concluded in the 1951 Opinion that the legislative authority of a municipal corporation could, if it deemed it necessary to the most advantageous sale of mortgage revenue bonds, pay out of the proceeds of the sale thereof a commission for the sale of such bonds.

With this conclusion I have no quarrel. It is not, however, determinative of the question here.

The grant of power in Section 12, Article XVIII, of the Constitution, carries its own limitation. By its terms the purposes for which mortgage bonds may be issued are the acquisition, construction or extension of any public utility. What has been said above with regard to the purposes for which general obligation bonds may be issued is pertinent here. While the situation giving rise to the moral obligation occurred in connection with the construction of a sewer system, the payment of this obligation is not necessary to the construction of the sewer system and can not now be considered a cost of acquiring, constructing or extending this improvement. Indeed, the theory is that this is a claim which is unenforceable as a cost of constructing the sewer, hence the moral obligation.

I am unable to find any authority for the issuance of obligations of indebtedness to secure funds to pay a moral obligation of a municipal corporation. Under the Uniform Bond Law a subdivision or other political taxing unit is limited in the purposes for which it may create or incur indebtedness. There is no statutory authority for issuing bonds in payment of moral obligations regardless of the nature of the transaction from which the moral obligation arose. Such an obligation can only be treated as a current operating expense of the municipality.

In answer to your question, therefore, I am of the opinion that:

1. The legislative authority of a village has the power to recognize as a moral obligation of the village interest payments and payments on principal received by the village on the credit of private individuals.

2. Such payments may be made directly to the lending institution.

3. The village may not, however, satisfy this moral obligation

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Respectfully,
WILLIAM B. SAXBE
Attorney General