INTERNATIONAL MUNICIPAL LAWYERS ASSOCIATION



Work Session II: Public Finance 101:
Debt, Elections, Securities, and Taxation

Title

"Fun"damentals in Municipal Securities

by

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The Municipals Securities Industry

State and local government financings of various projects have rapidly and consistently increased for more than a century and a half. Debt financing for municipalities has become acceptable and more common to support municipalities and their financing needs. The amount of state and local debt outstanding has expanded throughout the years and in 1900, state and local governments had borrowed $175 million from investors, bring the level of outstanding debt to more than $2 billion at that time.[1] In the 20th century, the total number of public offerings has continued to escalate. Total state and local debt outstanding reached $5 billion when the 16th Amendment to the United States Constitution established the federal income tax in 1913.[2] For the first time, interest on state and local securities issued were exempted from taxes and, as a direct result, interest rates on governmental securities dropped markedly when compared to rates on taxable corporate and federal securities. By 1950, there was about $24 billion of outstanding municipal securities and in 1966, new municipal issues totaled $17.6 billion and the amount of debt outstanding exceeded $105 billion. By 1971, the comparable figures were $50.6 billion and $161.8 billion, respectively.[3] In the most recent report from the United States Securities and Exchange Commission, Office of Municipal Securities on Transactions and Municipal Securities, dated July 1, 2004, the Office of Municipal Securities found that on November 5, 2000, there were about 51,000 issuers with outstanding municipal securities. These issuers had 1,100,000 outstanding municipal securities, with a principal amount of about $2.0 trillion dollars. The Bond Market Association's August 2004, newsletter entitled "Research," reported that for the 2004 second quarter, there were 3,831 long-term municipal general obligation issuances in the total amount of $67,246.3 million. For the same quarter, there were 2,983 long-term municipal revenue bond issuances in the amount of $122,726.3 million. As has been in the past, individuals hold the majority of these municipal securities either directly or through mutual funds.

Overview of Municipal Securities Laws

Unlike corporate securities, municipal securities are not subject to registration with the United States Securities and Exchange Commission ("SEC"). The disclosure of information regarding municipalities and their proposed issuance of securities to individual investors is at the core of the United States securities laws. The SEC does not participate in or approve the issuance of municipal securities, however, federal securities laws require that full and fair disclosure be made in order for an investor to make a decision as to whether to purchase municipal securities.

Section 17(a) of the Securities Act of 1933 ("1933 Act") and Section 10 of the Securities Exchange Act of 1934 ("1934 Act") set the legal standard for the disclosure of information to be made available to potential investors. The 1933 and 1934 Acts have two basic objectives:

1. material information about securities must be disclosed to allow investors to make informed decisions; and

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[1] Fundamentals of Municipal Bonds. Public Securities Association. 4th Edition.
[2] *Id.*
[3] *Id.*

2. misrepresentations or other fraudulent conduct in connection with the purchase and sale of securities is prohibited.

The first federal securities law adopted by Congress aimed to primarily curb abuses in the corporate securities market was the 1933 Act. The 1933 Act exempted municipal securities from the rigorous registration requirements imposed on issuers of corporate securities; however, municipal securities were not exempt from the anti-fraud provisions of securities laws. The broad language and remedial purposes of federal securities anti-fraud laws have evolved primarily through judicial interpretation. Additionally, the activities of municipal securities brokers and dealers are regulated by the SEC and also by the "Municipal Securities Rule-Making Board," all created in 1975 under an Amendment to the 1934 Act.

As previously noted, the volume of investments in the municipal securities market has increased dramatically and, along with the increased volume, certain perceived abuses in the municipal securities market have been brought to light. In the 1970's, the financial crisis of the City of New York, followed by a default on over $2 billion in bonds by the Washington Public Power Supply System in the 1980's, have brought attention and increased regulation of municipal securities. Upon the completion of its review of the Washington Public Power Supply System and its default, the SEC adopted Section 240.15c2-12 ("Rule 15c2-12"). Rule 15c2-12 became effective January 1, 1990, and has increased the focus of securities laws, particularly with respect to disclosure matters. In the mid-1990's, the SEC adopted new secondary market disclosure rules by amending Rule 15c2-12. The new amendments require certain municipal issuers to undertake annual disclosure updates as well as prompt disclosure of specific material events related to post-issuance events. ***Rule 15c2-12 is discussed and presented below.***

The anti-fraud provisions promulgated by the 1933 and 1934 Acts apply to every participant in all of the securities markets in the United States. As noted, corporate securities offerings are also subject to the requirement of registration with the SEC in addition to the anti-fraud provisions applicable to municipal issuers. Corporate issuers must generally make quarterly periodic filings with the SEC and must also file their prospectus with the SEC before issuing securities. Corporate issuers are subject to many detailed rules regarding the issuance of securities that are sometimes called "checklists." Because of the political and constitutional history of this country regarding municipal securities, different disclosure requirements for municipal security issuers have developed. The SEC cannot impose detailed rules as to the format and content of disclosure for municipal securities issuances. Although there is no official "checklist" for municipal issuers regarding market disclosures as there is for corporate issuers, the concepts of materiality, accuracy, and completeness found in the 1933 and 1934 Acts still control.

Securities laws are based upon making full and fair disclosure to purchasers of municipal securities to allow those individuals to make their own decisions regarding the purchase of investments. Financial and other pertinent information regarding a municipal issuer's securities should be made based on full and adequate disclosure. The information and data to be disclosed depends on the facts and circumstances of each municipal issuance. The fundamental, common-sense question that participants may employ in the preparation of an offering document for a municipal security is to ask, "What would I need to know if I was interested in buying these

securities?" If there is some information or data that one would want to have before making an investment in these municipal securities, more than likely, that information should be disclosed.

Issuance of Municipal Securities

One of the first steps needed to prepare for the issuance of municipal securities is to prepare a document making full disclosure to the prospective bond purchasers regarding the securities. This document is called an "official statement" or disclosure document. ***Please see attached Appendix A for a copy of certain pages to an offering document or official statement.*** Although various parties may be involved in preparing this official statement, including counsel to the underwriter, bond counsel, the issuer's financial advisor, disclosure counsel, or the staff of the municipality, the official statement is legally and ultimately the issuer's document. Final responsibility to meet existing and pertinent securities laws regarding disclosure requirements rests on the issuer and the issuer may be subject to liability for non-adherence to these laws. Additionally, persons or parties retained or working with the issuer in the issuance of securities may be held liable for violations of securities laws and may be imposed fines and obligated to pay damages to persons defrauded. ***For a discussion of certain participants and their roles in assisting with the issuance of municipal securities, see below.*** The basic standard for the preparation of official statements requires the use of accurate and true statements of material fact and prohibits that a material fact be omitted. Furthermore, statements and materials in the official statement may not be misleading. Information that is material must be disclosed if that information, if omitted, would have an impact on a "reasonable investor" in his final determination of whether to purchase a security.

As noted, officials of the issuer who approve the issuance of bonds and/or the offering documents along with other participants who assist in the issuance of obligations and the preparation of official statements have personal responsibility under federal securities laws. Public officials may not authorize the use of official statements or offering documents that they know to be materially false and misleading. Furthermore, public officials may not recklessly disregard facts that may indicate than an official statement runs the risk of disclosing misleading facts. Public officials may rely on consultants, financial advisors, and lawyers; however, that reliance must be reasonable. Public officials ultimately must be cognizant of any potential liability that may exists in presenting false and misleading statements in an offering document.

Continuing Disclosure

A municipal security purchaser's interest in factual and material information is pertinent not only at the initial purchase of the securities, but continues throughout the life of the obligation. Investors who did not buy a municipal security at the initial or primary offering may purchase those securities in the secondary market. Purchasers in the secondary market should have the same factual financial information to make an investment decision as initial purchasers in a primary offering. Investors in the secondary market attach great significance to a municipality's continuing disclosure and often rely on that continuing disclosure to be able to make a reasonable investment decision.

The anti-fraud provisions of the securities laws apply to all markets at all times. The SEC has adopted Rule 15c2-12 that also addresses disclosure in the municipal market. Rule 15c2-12 applies to both initial issuances and secondary market disclosure. In the initial issuance, the rule requires that an underwriter enter into a contract with a municipal issuer specifying that the municipality will furnish the underwriter disclosure documents and that the underwriter must file those statements with certain repositories. The required undertakings by the municipality must be contained in a written agreement or contract for the benefit of the holders of the securities. The most likely place to include this contract is in the municipality's ordinance or resolution authorizing the issuance of these securities, an indenture, trust agreement, a separate agreement between the issuer and the trustee or an undertaking by the issuer which specifically recites that it is for the benefit of the securities holders. ***Attached as Appendix B is a copy of certain pertinent pages of an ordinance authorizing the issuance of certificates and the required provisions needed to satisfy the requirements of Rule 15c2-12.***

Rule 15c2-12 also requires that the contract provide for disclosure to the secondary market on a continuing basis so long as the particular municipal securities are outstanding. The rule prohibits an underwriter from purchasing or selling municipal securities unless the municipality has entered into an agreement (as noted above) to make certain ongoing financial and operating information available to purchasers of municipal securities through a designated repository. ***For more information regarding Rule 15c2-12 and other related SEC provisions, please see below.***

Related Basic SEC Provisions[4]

In order to provide a more complete list of SEC requirements and their relevance to municipal securities and disclosure, the following recitation of Basic SEC Provisions is provided:

1. Section 3(a)(2) of the 1933 Act

   Except as herein expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

   3(a)(2) Any security issued or guaranteed by the United States or any territory thereof, or by the District of Columbia, or by any State of the United States, or by any political subdivision of a State or Territory, or by any public instrumentality of one or more States or Territories, or by any person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing; or any security issued or guaranteed by any bank . . . or any security which is an industrial development bond (as defined in Section 103(c)(2) of the Internal Revenue Code of 1954) the interest on which is excludable from gross income under Section 103(a)(1) of such Code if, by reason of the application of paragraph (4) or (6) of Section 103(c) of such Code (determined as if paragraphs (4)(A), (5), and (7) were not

[4] National Association of Bond Lawyers Resource Library

included in such Section 103(c)), paragraph (1) of such Section 103(c) does not apply to such security . . . .

2. Rule 131. Definition of Security Issued Under Government Obligations

a. Any part of an obligation evidenced by any bond, note, debenture, or other evidence of indebtedness issued by any governmental unit specified in Section 3(a)(2) of the Act which is payable from payments to be made in respect of property or money which is or will be used, under a lease, sale, or loan arrangement, by or for industrial or commercial enterprise, shall be deemed to be a separate "security" within the meaning of Section 2(1) of the Act, issued by the lessee or obligor under the lease, sale or loan arrangement.

b. An obligation shall not be deemed a separate "security" as defined in paragraph (a) hereof if,

1. the obligation is payable from the general revenues of a governmental unit, specified in Section 3(a)(2) of the Act, having other resources which may be used for payment of the obligation, or

2. the obligation relates to a public project or facility owned and operated by or on behalf of an under the control of a governmental nit specified in such Section, or

3. the obligation relates to a facility which is leased to and under the control of an industrial or commercial enterprise but is a part of a public project which, as a whole, is owned by and under the general control of a governmental unit specified in such Section, or an instrumentality thereof.

3. Section 17(a) of the 1933 Act

Section 17. (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly:

1. to employ any device, scheme, or artifice to defraud, or

2. to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made in the light of the circumstances under which they were made, not misleading, or

3. to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

4. Section 10(b) of the 1934 Act

Section 10. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange,

b. To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

5. Rule 10b-5

Rule 10b-5. Employment of Manipulative and Deceptive Devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of a national securities exchange,

1. to employ any device, scheme or artifice to defraud,

2. to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

3. to engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

6. Rule 15c2-12

Rule 15c2-12 "was designed to establish standards for the procurement and dissemination by underwriters of disclosure documents as a means of enhancing the accuracy and timeliness of disclosure to investors in municipal securities."[5]

SEC Adopted Regulatory Amendments to Rule 15c2-12 which, subject to certain exemptions, require municipal underwriters to obtain commitments from municipal issuers or "obligated persons" for ongoing annual and event-related

[5] Release No. 34-26985, June 28, 1989 (the "Final Release"), 54 Fed. Reg. 28799 at 28800. The Final Release also announced the adoption of Rule 15c2-12, explained changes made to the proposed Rule and modified the earlier Release.

disclosure before participating in the primary offering.[6] The obligations of municipal issuers to provide initial and ongoing disclosure are imposed by a contractual undertaking between the issuer and its underwriters which the Rule requires underwriters to obtain. ***See Appendix B herein for a sample copy of an ordinance providing for this contractual obligation.*** Under Rule 15c2-12, the underwriter must:

1. obtain and review an official statement that, except for certain specified information, is "deemed final" by an issuer prior to making a bid for, or purchase, offer or sale of municipal securities;

2. in negotiated sales, provide the most recent preliminary official statement (if one exists) upon request by a potential customer;

3. contract to receive, within a specified time, sufficient copies of the final official statement to comply with the fourth requirement; and

4. deliver, upon request by a potential customer, copies of the final official statement for a specified time period.[7]

The Rule was amended to prohibit municipal securities dealers or brokers to purchase or sell municipal securities in connection with a primary offering (covered by the Rule) unless the issuer of municipal securities has agreed in writing to provide for the benefit of holders of securities the following:

1. annual reports to each nationally recognized municipal securities information repository ("NRMSIR") and to any applicable state information depository ("SID"), financial information and operating data of the type provided in the final official statement (***see Appendix C for listing of NRMSIRs and SIDs***);

2. audited financial statements for each such obligated person, but only when available, to each NRMSIR and applicable SID; and

3. notices of eleven (11) specified events, if material, to each NRMSIR or the Municipal Securities Rule-Making Board and to any applicable SID.

Exemptions

The amendments, like the Rule, do not apply to offerings of less than $1 million in principal amount. Additionally, exceptions exist for:

1. offerings of securities with minimum denominations of $100,000 or more under certain circumstances;

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[6] Exchange Act Release No. 34-34961, November 19, 1994 (the "Amendments")
[7] 54 FR 28799

2. offerings of securities with a term of 18 months or less, but not from an agreement to provide material event notices;

3. offerings of securities from the agreement to provide annual financial information and operating data and audited financial statements, but no the agreement to provide material event notices, if after the offering, the municipality does not have more than $10 million aggregate principal amount of outstanding municipal securities, excluding securities exempted by the existing rule; and

4. the municipal issuer has agreed, for the benefit of the security holders, to provide, either on request to any person or annually to any SID, all financial information and operating data that is customarily prepared by such municipality and is publicly available.

Participants and Their Roles in Municipal Securities Financing

In order to offer a listing of certain participants and their contributions to municipal securities issuances, the following information is provided:

Issuers

The main participants in the offering of municipal securities is the issuer of the securities. In a municipal securities offering, the issuer will be a state, a county, a city, school district, or other political subdivision authorized to issue municipal securities. Another governmental issuer may be a special purpose public authority that issues securities on behalf of a governmental issuer. The disclosure responsibility of a municipal issuer will vary depending on the offering being undertaken. When a municipal issuer is the primary obligor, significant disclosure responsibilities and liabilities will be borne by the municipality.

Underwriters

Municipal issuers may sell securities to the underwriter through a competitive bidding process or a negotiation process. Public sales are governed by state and local laws. The underwriter will provide the necessary funds for certain municipal projects. Underwriters have well-established responsibilities in primary offerings of municipal securities.

Financial Advisors

The financial advisor is generally an independent firm that assists the municipal issuer in a public offering. A financial advisor will assist and give advice in the structuring of a financial transaction and provide assistance in the collection and preparation of data and information needed for inclusion in a municipal issuer's disclosure document.

Credit Enhancer

In certain municipal issuances, a credit enhancer is asked to participate. Such credit enhancer includes a bond insurer or a financial institution issuing a supporting letter of credit. A credit enhancer is utilized generally to provide interest savings as a result of an improved credit rating by the purchase of bond insurance or to obtain a special financing that would not be available with a credit enhancement.

Trustee

In certain municipal issuances generally involving revenue bonds, a trustee is appointed under a bond resolution or trust indenture. Trustees may also provide registration and paying agent functions and may also represent bond holders in the event of a default. Trustees may also collect and accept information and materials for the bond holders while the securities are outstanding.

Bond Counsel

Bond counsel represent the issuer in the review and interpretation of applicable laws and assists in the preparation of necessary documents for municipal proceedings. Bond counsel also prepares other legal documents necessary to validate municipal obligations and give assurance to investors that the securities are valid and enforceable. Bond counsel renders a legal opinion as to the validity and enforceability of the securities. With the advent of the federal income tax and the exemption of taxation of certain interest earned from municipal securities, bond counsel is asked to opine as to the tax exemption of interest earned on a particular offering. Bond counsel may also draft appropriate resolutions of meetings of the issuer's governing body at which authorization for the issuance of municipal securities is obtained.

Underwriter's Counsel

Separate legal counsel representing underwriters are often employed in certain municipal financings. Although the disclosure or offering document represents and belongs to the issuer, underwriter's counsel often serve as initial coordinators of the disclosure document. Underwriter's counsel assist the underwriter in performing its "due diligence" investigation of the municipal issuer, the project being financed, and the security pledge for repayment of the obligation. Underwriter's counsel seeks to confirm the basis of bond council opinion to ensure that the opinion addresses the necessary issues needed in the transaction so that the underwriter may reasonably rely on the opinion.

Issuer's Counsel

A full-time city attorney or other governmental attorney, or a private law firm may act as counsel to the issuer. Issuer's counsel provides invaluable assistance in gathering information about the issuer and in certain procedural matters relating to the issuance of municipal securities. Generally, issuer's counsel is expected to give an opinion as to the organization and good standing of the municipality, the municipality's authority and power to enter into the financial

transaction, the incumbency of the municipal officials, the adoption and validity of pertinent documents, and may be further asked to opine as to any pending or threatening litigation that exists (or does not exist) that may have an impact on the municipality's ability to comply with its contractual obligations in the issuance of a municipal security. Issuer's counsel may assume the responsibility for determining the legal existence of an issuer and the authority to engage in the financial transaction and to provide insight into potential difficulties and appropriate actions needed prior to the issuance of municipal securities.

Conclusion

Factual and complete disclosure of information that is material to an investment in a municipal security is essential to a prospective purchaser of securities. An investor's consideration of a purchase of a municipal security is dependent upon pertinent and truthful information that is uniquely under the control of the municipality. Protection from misleading information or the omission of material statements is paramount to the continued growth of the municipal securities market and the ability of municipalities to finance their much needed projects.

APPENDIX A

OFFICIAL STATEMENT
Dated March 18, 2004

NEW ISSUE – BOOK-ENTRY-ONLY

RATINGS: Fitch: "AAA"
Moody's: "Aaa"
S&P: "AAA"
(See "RATINGS" and "BOND INSURANCE" herein.)

In the opinion of Co-Bond Counsel, Fulbright & Jaworski L.L.P., San Antonio, Texas, and Escamilla & Poneck, Inc., San Antonio, Texas, under existing statutes, regulations, rulings, and case law, interest on the 2004 Refunding Bonds is includable in the gross income of the owners thereof for federal income tax purposes. Co-Bond Counsel express no opinion regarding any other tax consequences related to the purchase, ownership or disposition of, or the accrual or receipt of interest on, the 2004 Refunding Bonds. See "TAX MATTERS" herein.

$13,245,000
CITY OF SAN ANTONIO, TEXAS
Taxable General Improvement Refunding Bonds, Series 2004

Date: March 1, 2004

Due: February 1, as shown herein

The $13,245,000 "City of San Antonio, Texas Taxable General Improvement Refunding Bonds, Series 2004" (the "2004 Refunding Bonds") are being issued by the City of San Antonio, Texas (the "City") pursuant to the Constitution and general laws of the State of Texas, particularly Chapter 1207, Texas Government Code, as amended; the Home Rule Charter of the City (the "City Charter"); and an ordinance (the "Ordinance") adopted by the City Council of the City (the "City Council") on March 18, 2004. (See "THE 2004 REFUNDING BONDS - Authority for Issuance" herein.)

Interest on the 2004 Refunding Bonds will accrue from March 1, 2004 and will be payable on February 1 and August 1 of each year, commencing August 1, 2004, and will be calculated on the basis of a 360-day year composed of twelve 30-day months. The 2004 Refunding Bonds will be issued as fully registered obligations in book-entry-only form and when issued will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository (the "Securities Depository"). Book-entry interests in the 2004 Refunding Bonds will be made available for purchase in the principal amount of $5,000 or any integral multiple thereof. Purchasers of the 2004 Refunding Bonds (the "Beneficial Owners") will not receive physical delivery of certificates representing their interest in the 2004 Refunding Bonds. So long as the Securities Depository is the registered owner of the 2004 Refunding Bonds, the principal of and interest on the 2004 Refunding Bonds will be payable by JPMorgan Chase Bank, Dallas, Texas, as the initial Paying Agent/Registrar, to the Securities Depository, which will in turn remit such principal and interest to its participants, which will in turn remit such principal and interest to the Beneficial Owners. (See "THE 2004 REFUNDING BONDS - Book-Entry-Only System" herein.)

The 2004 Refunding Bonds are payable from annual ad valorem taxes levied against all taxable property located within the City, within the limitations prescribed by law, including the constitutional tax limit of $2.50 per $100 of assessed valuation. (See "THE 2004 REFUNDING BONDS – Security" herein.)

Proceeds of the 2004 Refunding Bonds will be used to refund certain of the City's outstanding general obligation indebtedness in which the proceeds thereof were used to finance or refinance certain parking facilities owned and operated by the City. Refunding such obligations with the 2004 Refunding Bonds, which are taxable obligations, is being undertaken to provide greater flexibility for the City to contract with private entities for use of space in those facilities.

Concurrently with the sale of the 2004 Refunding Bonds, the City will separately sell its "City of San Antonio, Texas General Improvement Bonds, Series 2004" and "City of San Antonio, Texas Combination Tax and Revenue Certificates of Obligation, Series 2004" in the aggregate principal amount of $63,095,000 (collectively, the "2004 Obligations"). This Official Statement describes the 2004 Refunding Bonds, but not the 2004 Obligations.

FSA The scheduled payment of principal of and interest on the 2004 Refunding Bonds when due will be guaranteed under an insurance policy issued concurrently with the delivery of the 2004 Refunding Bonds by FINANCIAL SECURITY ASSURANCE INC.

SEE INSIDE COVER PAGE FOR STATED MATURITIES, PRINCIPAL AMOUNTS, INTEREST RATES, INITIAL YIELDS, CUSIP NUMBERS, AND REDEMPTION PROVISIONS FOR THE 2004 REFUNDING BONDS

The 2004 Refunding Bonds are offered for delivery, when, as and if issued and received by the initial purchasers (the "Underwriters"), and subject to the approving opinion of the Attorney General of the State of Texas and the approval of certain legal matters by Fulbright & Jaworski L.L.P., San Antonio, Texas and Escamilla & Poneck, Inc., San Antonio, Texas as Co-Bond Counsel. Certain legal matters will be passed upon for the Underwriters by their legal counsel, McCall, Parkhurst & Horton L.L.P., San Antonio, Texas, and for the City by the City Attorney. (See "LEGAL MATTERS" herein.) It is expected that the 2004 Refunding Bonds will be available for initial delivery through the services of DTC on or about April 13, 2004.

FIRST SOUTHWEST COMPANY
M. E. Allison & Co., Inc.

Southwestern Capital Markets, Inc.

RAMIREZ & CO., INC.
Southwest Securities

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The cover page, subsequent pages hereof, and appendices attached hereto, are part of this Official Statement.

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Undertakings" as to which no opinion is expressed) to determine whether such information fairly summarizes the material and documents referred to therein and is correct as to matters of law. Co-Bond Counsel have not, however, independently verified any of the factual information contained in this Official Statement nor has it conducted an investigation of the affairs of the City for the purpose of passing upon the accuracy or completeness of this Official Statement. No person is entitled to rely upon Co-Bond Counsel's limited participation as an assumption of responsibility for, or an expression of opinions of any kind with regard to the accuracy or completeness of any of the information contained herein. The legal fees to be paid Co-Bond Counsel for services rendered in connection with the issuance of the 2004 Refunding Bonds are contingent on issuance and delivery of the 2004 Refunding Bonds. The legal opinions of Co-Bond Counsel will accompany the obligations deposited with DTC or will be printed on the definitive obligations in the event of the discontinuance of the Book-Entry-Only System. Certain legal matters will be passed upon for the Underwriters by their counsel, McCall, Parkhurst & Horton L.L.P., San Antonio, Texas.

The various legal opinions to be delivered concurrently with the delivery of the 2004 Refunding Bonds express the professional judgment of the attorneys rendering the opinions as to the legal issues explicitly addressed therein. In rendering a legal opinion, the attorney does not become an insurer or guarantor of that expression of professional judgment, of the transaction opined upon, or of the future performance of the parties to the transaction. Nor does the rendering of an opinion guarantee the outcome of any legal dispute that may arise out of the transaction.

RATINGS

Moody's Investors Service, Inc. ("Moody's"), Standard & Poor's Ratings Services, a Division of the McGraw-Hill Corporation ("S&P"), and Fitch Ratings, Inc. ("Fitch") have assigned their municipal bond ratings of "Aaa," "AAA," and "AAA," respectively, to the 2004 Refunding Bonds, as a result of a municipal bond insurance policy issued by Financial Security Assurance Inc. See "BOND INSURANCE" herein. The City's unenhanced general obligation debt is rated "Aa2," "AA+," and "AA+" by Moody's, S & P, and Fitch. An explanation of the significance of such ratings may be obtained from Moody's, S&P, or Fitch. The rating of the 2004 Refunding Bonds by Moody's, S&P, and Fitch reflects only the views of said companies at the time the ratings are given, and the City makes no representations as to the appropriateness of the ratings. There is no assurance that the ratings will continue for any given period of time, or that the ratings will not be revised downward or withdrawn entirely by Moody's, S&P, and Fitch if, in the judgment of said companies, circumstances so warrant. Any such downward revision or withdrawal of the ratings may have an adverse effect on the market price of the 2004 Refunding Bonds.

CONTINUING DISCLOSURE OF INFORMATION

In the Ordinance, the City has made the following agreement for the benefit of the holders and Beneficial Owners of the 2004 Refunding Bonds. The City is required to observe the agreement for so long as it remains obligated to advance funds to pay the 2004 Refunding Bonds. Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified material events, to certain information vendors. This information will be available to securities brokers and others who subscribe to receive the information from the vendors.

Annual Reports

Under Texas law, including, but not limited to, Chapter 103, Texas Local Government Code, as amended, the City must keep its fiscal records in accordance with generally accepted accounting principles, must have its financial accounts and records audited by a certified public accountant and must file each audit report with the City Clerk. The City's fiscal records and audit reports are available for public inspection during the regular business hours of the City Clerk. Additionally, upon the filing of these financial statements and the annual audit, these documents are subject to the Texas Open Records Act, Texas Government Code, Chapter 552, as amended. Thereafter, any person may obtain copies of these documents upon submission of a written request to the City Clerk, City of San Antonio, Texas, 100 Military Plaza, San Antonio, Texas 78205, and upon paying the reasonable copying, handling, and delivery charges for providing this information.

The City will provide certain updated financial information and operating data to certain information vendors annually. The information to be updated includes all quantitative financial information and operating data with respect to the City

of the general type included in this Official Statement indicated as Tables 1-14 and 16-19, and in Appendix B. The City will update and provide this information within six months after the end of each fiscal year. The City will provide the updated information to each nationally recognized municipal securities information repository ("NRMSIR") and to any State Information Depository ("SID").

The City may provide updated information in full text or may incorporate by reference certain other publicly available documents, as permitted by the Rule. The updated information will include audited financial statements, if the City commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the City will provide unaudited information within the required time and audited financial statements when and if the audit report becomes available. Any such financial statements will be prepared in accordance with the accounting principles described in Appendix B or such other accounting principles as the City may be required to employ from time to time pursuant to State law or regulation.

The City's fiscal year ends September 30. Accordingly, it must provide updated information by March 31 in each year, unless the City changes its fiscal year. If the City changes its fiscal year, it will notify each NRMSIR and any SID of the change.

Material Event Notices

The City will also provide timely notices of certain events to certain information vendors. The City will provide notice of any of the following events with respect to the 2004 Refunding Bonds, if such event is material to a decision to purchase or sell 2004 Refunding Bonds: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the status of the 2004 Refunding Bonds; (7) modification to rights of holders of the 2004 Refunding Bonds; (8) bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the 2004 Refunding Bonds; and (11) rating changes. (Neither the 2004 Refunding Bonds nor the Ordinance make any provision for debt service reserves or liquidity enhancement.) In addition, the City will provide timely notice of any failure by the City to provide information, data, or financial statements in accordance with its agreement described above under "Annual Reports." The City will provide each notice described in this paragraph to any SID and to either each NRMSIR or the Municipal Securities Rulemaking Board ("MSRB").

Availability of Information from NRMSIRs and SID

The City has agreed to provide the foregoing information only to NRMSIRs and any SID. The information will be available to holders of the 2004 Refunding Bonds only if the holders comply with the procedures and pay the charges established by such information vendors or obtain the information through securities brokers who do so.

The Municipal Advisory Council of Texas has been designated by the State as a SID. The address of the Municipal Advisory Council is 600 West 8th Street, Austin, Texas 78701, or Post Office Box 2177, Austin, Texas 78768-2177 and its telephone number is (512) 476-6947.

Limitations and Amendments

The City has agreed to update information and to provide notices of material events only as described above. The City has not agreed to provide other information that may be relevant or material to a complete presentation of its financial results of operations, condition, or prospects or agreed to update any information that is provided, except as described above. The City makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell 2004 Refunding Bonds at any future date. The City disclaims any contractual or tort liability for damages resulting in whole or in part from any breach of its continuing disclosure agreement or from any statement made pursuant to its agreement, although holders of the 2004 Refunding Bonds may seek a writ of mandamus to compel the City to comply with its agreement.

This continuing disclosure agreement may be amended by the City from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of

operations of the City, but only if (1) the provisions, as so amended, would have permitted an underwriter to purchase or sell the 2004 Refunding Bonds in the primary offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule since such offering, as well as such changed circumstances; and (2) either (i) the registered owners of a majority in aggregate principal amount (or any greater amount required by any other provision of the Ordinance that authorize such an amendment) of the outstanding 2004 Refunding Bonds consent to such amendment or (ii) a person that is unaffiliated with the City (such as nationally recognized bond counsel) determined that such amendment will not materially impair the interest of the registered owners and Beneficial Owners of the 2004 Refunding Bonds. The City may also repeal or amend the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provision of the Rule or a court of final jurisdiction enters judgment that such provisions of the Rule are invalid, but only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling 2004 Refunding Bonds in the primary offering of the 2004 Refunding Bonds.

Compliance with Prior Undertakings

The City has complied in all material respects with all of its previous continuing disclosure agreements in accordance with the Rule.

FORWARD-LOOKING STATEMENTS

The statements contained in this Official Statement, and in any other information provided by the City, that are not purely historical, are forward-looking statements, including statements regarding the City's expectations, hopes, intentions, or strategies regarding the future. Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the City on the date hereof, and the City assumes no obligation to update any such forward-looking statements. The City's actual results could differ materially from those discussed in such forward-looking statements.

The forward-looking statements included herein are necessarily based on various assumptions and estimates and are inherent subject to various risks and uncertainties, including risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes or developments in social, economic, business, industry, market, legal, regulatory circumstances and conditions and actions taken or omitted to be taken by third parties, including customers, suppliers, business partners and competitors, and legislative, judicial, and other governmental authorities and officials. Assumptions related to the foregoing involve judgments with respect to, among other things, future economic, competitive, and market conditions of future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the City. Any of such assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Official Statement will prove to be accurate.

UNDERWRITING

The Underwriters have agreed, subject to certain conditions, to purchase the 2004 Refunding Bonds from the City at a purchase price of $13,158,646.70 plus accrued interest. The Underwriters' obligations are subject to certain conditions precedent, and they will be obligated to purchase all of the 2004 Refunding Bonds if any 2004 Refunding Bonds are purchased. The 2004 Refunding Bonds may be offered and sold to certain dealers and others at prices lower than such public offering prices, and such public prices may be changed from time to time by the Underwriters.

The Underwriters have reviewed the information in the Official Statement in accordance with their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

CO-FINANCIAL ADVISORS

Coastal Securities and Estrada Hinojosa & Company, Inc. (the "Co-Financial Advisors") are employed by the City in connection with the issuance of the 2004 Refunding Bonds and, in such capacity, have assisted the City in the

APPENDIX B

CITY OF HOUSTON ORDINANCE NO. 2004-____

AN ORDINANCE AUTHORIZING ISSUANCE OF CITY OF HOUSTON, TEXAS, PUBLIC IMPROVEMENT REFUNDING BONDS, SERIES 2004B; PRESCRIBING THE TERMS AND FORM THEREOF; PROVIDING FOR THE PAYMENT OF THE PRINCIPAL THEREOF AND INTEREST THEREON; AUTHORIZING THE MAYOR AND CITY CONTROLLER TO ACCEPT AND EXECUTE THE WINNING BID FOR THE BONDS, APPROVE THE AMOUNTS, INTEREST RATES, PRICES AND TERMS OF SUCH BONDS, THE NOTES TO BE REFUNDED THEREBY AND CERTAIN OTHER MATTERS RELATED THERETO; AUTHORIZING THE PURCHASE OF A POLICY OF MUNICIPAL BOND INSURANCE; RATIFYING THE USE OF A PRELIMINARY OFFICIAL STATEMENT AND OFFICIAL NOTICE OF SALE AND AUTHORIZING THE PREPARATION AND DISTRIBUTION OF AN OFFICIAL STATEMENT TO BE USED IN CONNECTION WITH THE SALE OF THE BONDS; AUTHORIZING THE DEFEASANCE OF OUTSTANDING NOTES, THE EXECUTION AND DELIVERY OF AN ESCROW AGREEMENT, THE PURCHASE OF AND SUBSCRIPTION FOR CERTAIN SECURITIES AND THE USE OF CERTAIN FUNDS RELATED TO THE NOTES TO BE DEFEASED; AUTHORIZING ESCROW VERIFICATION; MAKING OTHER PROVISIONS REGARDING SUCH BONDS AND MATTERS INCIDENT THERETO; AUTHORIZING EXECUTION AND DELIVERY OF A PAYING AGENT/REGISTRAR AGREEMENT, A CO-BOND COUNSEL AGREEMENT AND SPECIAL DISCLOSURE CO-COUNSEL AGREEMENT; AND DECLARING AN EMERGENCY

BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF HOUSTON:

ARTICLE I

FINDINGS AND DETERMINATIONS

Section 1.1: Findings and Determinations. It is hereby officially found and determined that:

(a) The City of Houston, Texas (the *"City"*) has issued certain general obligation commercial paper notes to be further described in the Officers' Pricing Certificate (as defined herein) (the *"Refunded Notes"*).

(b) The City is authorized by Chapter 1207, Texas Government Code, as amended (hereinafter in this Article *"Chapter 1207"*) to issue its Public Improvement Refunding Bonds, Series 2004B (the *"Series 2004B Bonds"*) for, among other purposes, the purpose of refunding and defeasing the Refunded Notes.

(c) The City desires and intends to refund and redeem the Refunded Notes in order to provide financing at fixed rates for the permanent improvements, public works and equipment initially financed with the proceeds of the Refunded Notes and not for the purpose of realizing present value savings.

(d) The City has determined that the issuance of the Series 2004B Bonds to refund the Refunded Notes is in the best interest of the City, although the manner in which the refunding of the

General's approval and as he determines are consistent with the intent and purposes of this Ordinance, which determination shall be final.

ARTICLE VIII
CONTINUING DISCLOSURE UNDERTAKING

Section 8.1: Annual Reports. The City shall provide annually to each NRMSIR and any SID, within six months after the end of each fiscal year, financial information and operating data with respect to the City of the general type included in the final Official Statement authorized by Section 7.3 of this Ordinance, being the information described in Exhibit H hereto. Any financial statements so to be provided shall be (1) prepared in accordance with the accounting principles described in Exhibit H hereto and (2) audited, if the City commissions an audit of such statements and the audit is completed within the period during which they must be provided. If audited financial statements are not so provided, then the City shall provide audited financial statements for the applicable fiscal year to each NRMSIR and any SID, when and if audited financial statements become available but if such audited financial statements are unavailable the City will provide such financial statements on an unaudited basis within the above-described six-month period.

If the City changes its fiscal year, it will notify each NRMSIR and any SID of the change (and of the date of the new fiscal year end) prior to the next date by which the City otherwise would be required to provide financial information and operating data pursuant to this Section.

The financial information and operating data to be provided pursuant to this Section may be set forth in full in one or more documents or may be included by specific reference to any document (including an official statement or other offering document, if it is available from the MSRB) that theretofore has been provided to each NRMSIR and any SID or filed with the SEC, or may be provided in any other manner consistent with the Rule.

Section 8.2: Material Event Notices. The City shall notify any SID and either each NRMSIR or the MSRB, in a timely manner, of any of the following events with respect to the Series 2004B Bonds, if such event is material within the meaning of the federal securities laws:

A. Principal and interest payment delinquencies;

B. Non-payment related defaults;

C. Unscheduled draws on debt service reserves reflecting financial difficulties;

D. Unscheduled draws on credit enhancements reflecting financial difficulties;

E. Substitution of credit or liquidity providers, or their failure to perform;

F. Adverse tax opinions or events affecting the tax-exempt status of the Series 2004B Bonds;

G. Modifications to rights of holders;

H. Bond calls;

I. Defeasances;

J. Release, substitution, or sale of property securing repayment of the Series 2004B Bonds; and

K. Rating changes.

The City shall notify any SID and either each NRMSIR or the MSRB, in a timely manner, of any failure by the City to provide financial information or operating data in accordance with Section 8.1 of this Ordinance by the time required by such Section.

Section 8.3: Limitations, Disclaimers, and Amendments. The City shall be obligated to observe and perform the covenants specified in this Article for so long as, but only for so long as, the City remains an "obligated person" with respect to the Series 2004B Bonds within the meaning of the Rule, except that the City in any event will give the notice required by Section 8.2 of any Series 2004B Bond calls and defeasance that cause the City to be no longer such an "obligated person."

The provisions of this Article are for the sole benefit of the Registered Owners and beneficial owners of the Series 2004B Bonds, and nothing in this Article, express or implied, shall give any benefit or any legal or equitable right, remedy, or claim hereunder to any other person. The City undertakes to provide only the financial information, operating data, financial statements, and notices which it has expressly agreed to provide pursuant to this Article and does not hereby undertake to provide any other information that may be relevant or material to a complete presentation of the City's financial results, condition, or prospects or hereby undertake to update any information provided in accordance with this Article or otherwise, except as expressly provided herein. The City does not make any representation or warranty concerning such information or its usefulness to a decision to invest in or sell Series 2004B Bonds at any future date.

UNDER NO CIRCUMSTANCES SHALL THE CITY BE LIABLE TO THE REGISTERED OWNER OR BENEFICIAL OWNER OF ANY SERIES 2004B BOND OR ANY OTHER PERSON, IN CONTRACT OR TORT, FOR DAMAGES RESULTING IN WHOLE OR IN PART FROM ANY BREACH BY THE CITY, WHETHER NEGLIGENT OR WITHOUT FAULT ON ITS PART, OF ANY COVENANT SPECIFIED IN THIS ARTICLE, BUT EVERY RIGHT AND REMEDY OF ANY SUCH PERSON, IN CONTRACT OR TORT, FOR OR ON ACCOUNT OF ANY SUCH BREACH SHALL BE LIMITED TO AN ACTION FOR MANDAMUS OR SPECIFIC PERFORMANCE.

No default by the City in observing or performing its obligations under this Article shall constitute a breach of or default under this Ordinance for purposes of any other provision of this Ordinance.

Nothing in this Article is intended or shall act to disclaim, waive, or otherwise limit the duties of the City under federal and state securities laws.

The provisions of this Article may be amended by the City from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the City, but only if (1) the provisions of this Article, as so amended, would have permitted an underwriter to purchase or sell Series 2004B Bonds in the primary offering of the Series 2004B Bonds in compliance with the Rule, taking into account any amendments or interpretations of the Rule to the date of such amendment, as well as such changed circumstances, and (2) either (a) the Registered Owners of a majority in aggregate principal amount (or any greater amount required by any other provision of this Ordinance that authorizes such an amendment) of the Outstanding Series 2004B Bonds consent to such amendment or (b) a person or entity that is unaffiliated with the City (such as nationally recognized bond counsel) determines that such amendment will not materially impair the interests of the Registered Owners and beneficial owners of the Series 2004B Bonds. If the City so amends the provisions of this Article, it shall include with any amended financial information or operating data next provided in accordance with Section 8.1 an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of financial information or operating data so provided. The City may also amend or repeal the provisions of this Article if the SEC amends or repeals the applicable provisions of the Rule or a court of final jurisdiction enters judgment that such provisions of the Rule are invalid, and the City also may amend the provisions of this Article in its discretion in any other manner or circumstance, but in either case only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling Series 2004B Bonds in the primary offering of the Series 2004B Bonds.

Section 8.4: Definitions.

As used in this Article, the following terms have the meanings ascribed to such terms below:

"MSRB" means the Municipal Securities Rulemaking Board.

"NRMSIR" means each person whom the SEC or its staff has determined to be a nationally recognized municipal securities information repository within the meaning of the Rule from time to time.

"Rule" means SEC Rule 15c2-12, as amended from time to time.

"SEC" means the United States Securities and Exchange Commission.

"SID" means any person designated by the State of Texas or an authorized department, officer, or agency thereof as, and determined by the SEC or its staff to be, a state information depository within the meaning of the Rule from time to time.

ARTICLE IX
MISCELLANEOUS

Section 9.1: Defeasance. The City may defease the provisions of this Ordinance and discharge its obligation to the Registered Owners of any or all of the Series 2004B Bonds to pay the principal of and interest thereon in any manner permitted by law, including by depositing

APPENDIX C



U.S. Securities and Exchange Commission

Municipal Securities Information Sources

Nationally Recognized Municipal Securities Information Repositories (NRMSIRs)

Bloomberg Municipal Repository

100 Business Park Drive
Skillman, New Jersey 08558
Phone: (609) 279-3225
Fax: (609) 279-5962
http://www.bloomberg.com/markets/rates/municontacts.html
Email: Munis@Bloomberg.com

DPC Data Inc.

One Executive Drive
Fort Lee, NJ 07024
Phone: (201) 346-0701
Fax: (201) 947-0107
http://www.dpcdata.com
Email: nrmsir@dpcdata.com

FT Interactive Data

Attn: NRMSIR
100 William Street
New York, New York 10038
Phone: (212) 771-6999
Fax: (212) 771-7390 (Secondary Market Information)
(212) 771-7391 (Primary Market Information)
http://www.interactivedata.com
Email: NRMSIR@FTID.com

Standard & Poor's Securities Evaluations, Inc.

55 Water Street
45th Floor
New York, NY 10041
Phone: (212) 438-4595
Fax: (212) 438-3975
www.jjkenny.com/jjkenny/pser_descrip_data_rep.html
Email: nrmsir_repository@sandp.com

State Information Depositories (SIDs)

Municipal Advisory Council of Texas

P.O. Box 2177
Austin, Texas 78768-2177

Phone: (512) 476-6947
Fax: (512) 476-6403
http://www.mactexas.com
Email for filings: mac@mactexas.com

Municipal Advisory Council of Michigan

1445 First National Building
Detroit, Michigan 48226-3517
Phone: (313) 963-0420
Fax: (313) 963-0943
http://www.macmi.com
Email for filings: mac@macmi.com

Ohio Municipal Advisory Council

9321 Ravenna Road, Unit K
Twinsburg, OH 44087-2445
Phone: (330) 963-7444
Toll-free: (800) 969-OMAC (6622)
Fax: (330) 963-7553
http://www.ohiomac.com
http://www.ohiosid.com
Email for filings: sid_filings@ohiomac.com

http://www.sec.gov/info/municipal/nrmsir.htm

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