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The Special Fund Doctrine and Revenue Bond Financing in South Carolina

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THE SPECIAL FUND DOCTRINE AND REVENUE BOND FINANCING IN SOUTH CAROLINA*

Public financing in South Carolina has grown tremendously in the last two decades. The rapid and steady expansion of the duties of government in South Carolina has resulted in state agencies and municipalities entering areas which were once deemed to be the concern only of private enterprise. Also, inflation has contributed its part toward increasing the cost of government. These conditions have meant that resort to private capital by state and local government through borrowing must be made more than ever before.

The issuance of millions of dollars of general obligation bonds has been accomplished in South Carolina by the use of the special fund doctrine.[1] Another means of obtaining money for public purposes since the beginning of the 1930's is by way of revenue bonds, which have had a spectacular growth in all states during the last few years.[2] The purpose of this article is to discuss revenue bond financing in South Carolina by first observing the Special Fund Doctrine as a background for the former and then to point out the constitutional problems which may arise when revenue bonds are issued.

Revenue bonds, as the term is used herein, are long term debt obligations issued for public projects secured solely by the revenue to be derived from the project undertaken.[3] Generally, in states other than South Carolina, no distinction is made between revenue bonds and so-called special fund bonds which are obligations payable solely out of a special fund.[4] However, the Special Fund Bond in South Carolina is actually a general obligation bond, for even though a special fund is primarily liable, the full faith, credit and taxing power of the governmental unit issuing the bond is also pledged to the payment of the debt.[5] "Special-general bond" would be a more descriptive term for the South Carolina Special Fund Bond for it

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1. Sinkler, *Constitutional Limitations on Public Finance in South Carolina,* 3 S. C. L. Q. 303 (1951).
2. Rose, *Developments in Revenue Bond Financing,* 6 U. FLA. L. REV. 385 (1953).
3. City of Spartanburg v. Blalock, 223 S.C. 253, 75 S.E. 2d 361, 365 (1953); 15 McQUILLEN, MUNICIPAL CORPORATIONS, § 43-11.
4. See Annot., 72 A.L.R. 687 (1931); 96 A.L.R. 1385 (1935); 146 A.L.R. 328 (1943).
5. *E. g.,* Briggs v. Greenville County, 137 S.C. 288, 135 S.E. 153 (1926); Evans v. Beattie, 137 S.C. 496, 135 S.E. 538 (1926).

would indicate the debt was a hybrid between a revenue bond and a general obligation bond.[6]

The leading case enunciating the Special Fund Doctrine is *State ex rel. Richards v. Moorer.*[7] The financing of highway construction was to be accomplished by the issuance of "evidences of indebtedness" to which were pledged both a special fund created from the gasoline tax and also the credit of the State. The court held that bonds secured by the pledge of a fund which might reasonably be expected to meet the obligations without the levy of a general property tax did not constitute bonded debt within the meaning of the Constitution, notwithstanding the fact that the full faith, credit and taxing power of the State were pledged.

In the *Moorer* opinion the court states that it has held a number of times that obligations of the same character as these bonds did not constitute a bonded debt within the meaning of the constitutional limitations.[8] Consequently, the origin of the Special Fund Doctrine would seem to be in the earliest of these cases, *Lillard v. Melton.*[9] A city issued "certificates of indebtedness" representing debts due by virtue of an assessment upon abutting property owners for part of the cost of street improvements. The assessments became liens upon the property which were pledged to the "certificates of indebtedness". The faith and credit of the city were also pledged to the obligations which could be used for the payment of debts or the obligations could be sold. The liens would presumably protect the city against loss upon its guaranty. The court did not discuss the ground for its decision, but held that the liability of the city on the guaranty of the paving assessments constituted only a contingent obligation and must be excluded from the constitutional limitations.[10]

It is difficult to understand the rationale behind a doctrine holding that obligations for which a municipality, county, or other governmental unit is ultimately liable would not be a "bonded debt" as the term is used within the Constitution. One readily observes that if the special fund proves insufficient to meet the payment of the prin-

6. Virtue, *The Public Use of Private Capital: A Discussion of Problems Related to Municipal Bond Financing,* 35 VA. L. REV. 285, 292 (1949).

7. 152 S.C. 455, 150 S.E. 269 (1929). The court states this proposition in State *ex rel.* Roddy v. Byrnes, 219 S.C. 485, 66 S.E. 33 (1951); also, see Sinkler, note 1 *supra* at 317.

8. 152 S.C. at 494, 150 S.E. at 282. These cases are Sullivan v. City Council of Charleston, 133 S.C. 189, 133 S.E. 340 (1925); Barnwell v. Matthews, 132 S.C. 314, 128 S.E. 712 (1925); McIntyre v. Rogers, 123 S.C. 334, 116 S.E. 277 (1923); Brownlee v. Brook, 107 S.C. 230, 92 S.E. 477 (1917); Lillard v. Melton, 103 S.C. 10, 87 S.E. 421 (1915).

9. Cited in note 8 *supra.*

10. *Id.* at 19, 87 S.E. at 425; see State *ex rel.* Richards v. Moorer, 152 S.C. at 497, 150 S.E. at 283.

cipal and interest as it becomes due, the bondholder will look to the general tax funds of the issuer for payment. Quite clearly the effect of the Special Fund Doctrine is to mitigate the debt limitations designed for the protection of the taxpayers of South Carolina. These limitations are succinctly stated below.

Article VIII, Section 7 of the South Carolina Constitution provides that no city shall incur a bonded debt which shall exceed eight per centum of the assessed value of the taxable property within the town. Article X, Section 5 sets forth an identical eight per cent limitation for counties, townships, school districts, or other political subdivisions. The latter section also provides that the aggregate debt over and upon any territory of the State shall never exceed fifteen per cent of the value of all taxable property in such territory.[11]

Even if the vigor of these limitations has been lost through the Special Fund Doctrine a governmental unit may not create bonded debt in any amount within its discretion simply by first creating a fund from excise taxes or other moneys and making it primarily liable for the payment of the debt. The court has recognized the danger inherent in the Special Fund Doctrine as originally enunciated for it has now held that the determination of the sufficiency of any special fund is in the nature of a judicial function.[12] This decision would apparently indicate that the court must give its approval upon the adequacy of any special fund created to secure general obligation bonds.[13]

The scheme of issuing general obligation bonds which are primarily secured by the pledging of a special fund deemed sufficient to meet the obligation has now been approved by the court so many times that it will never be modified because of stare decisis and the confusion which would ensue if overturned. Even in the *Moorer* decision[14] the court said, "To open the clear declarations of this court to doubt or question, after these millions of bonds have been issued in the state in reliance . . . upon these decisions, would seem almost inconceivable." The court again reiterates this view in *State ex rel. Roddy v. Byrnes*.[15] This was a proceeding wherein Special Fund Bonds issued for educational purposes and secured primarily by the

11. The court has developed the proposition that the fifteen per cent debt limit does not control the incurring of debt for counties, incorporated cities or towns and common school districts. An analysis of this doctrine would not seem to be relevant here. For a discussion of this topic, see Sinkler, *op. cit. supra* note 1.
12. Arthur v. Byrnes, 224 S.C. 51, 77 S.E. 2d 311 (1953).
13. Sinkler, *Constitutional Law*, 7 S. C. L. Q. 84 (1954).
14. 152 S.C. at 505, 150 S.E. at 286.
15. 219 S.C. 307, 66 S.E. 2d 33 (1951).

proceeds of a three per cent sales tax were held to be constitutional. This latter case is particularly interesting because of other observations which are made by the court. "In final analysis there should in good morals be little difference between our long-established . . . Special Fund Doctrine, and the contrary rule prevailing in other jurisdictions." But the court concludes by suggesting the real reason Special Fund Bonds have been utilized so frequently in South Carolina. "Nevertheless, the device is highly desirable because bond buyers pay higher prices for bonds in the nature of general obligations than for restricted revenue bonds."

Revenue Bond Financing

If the Special Fund Doctrine mitigated the protection offered taxpayers by constitutional debt limitations, the revenue bond, which is the full flower of the Special Fund Doctrine, completed the annihilation. Soon after the Revenue Bond Act[16] was passed in 1933 the court held in *Cathcart v. Columbia*[17] that revenue bonds, issued by a city pursuant to the Act, for the purpose of financing the construction of a stadium and payable solely out of revenue derived from the stadium project were constitutional. Since the city was not liable for any part of the debt and the general credit of the city was not pledged, the bonds were not debts within the meaning of the Constitution. The effect of the decision is that none of the constitutional debt limitations upon public financing are applicable to revenue bonds. Many other decisions have affirmed and approved this proposition.[18] One readily observes that in reality the only difference between Special Fund Bonds in South Carolina and revenue bonds is that payment of the special fund obligation is met through excise taxes and that payment of the revenue bond is achieved through a fund created from a fee for services rendered.

Other than circumventing debt limitations, revenue bonds offer other advantages. This type of financing provides services which directly and equitably relate benefits to burdens and seemingly at no cost to the taxpayer who pays only for his individual use and consumption. By emphasizing management, perhaps the powerful economic motives which work well in private enterprise have been utilized.[19]

16. CODE OF LAWS OF SOUTH CAROLINA, 1952 §§ 59-361 through 415. The Revenue Bond Act is occasionally referred to herein as "the Act".
17. 170 S.C. 362, 170 S.E. 435 (1933).
18. See *e. g.*, McNulty v. Owens, 188 S.C. 377, 199 S.E. 425 (1938); Park v. Greenwood County, 174 S.C. 35, 176 S.E. 870 (1934); Roach v. Columbia, 172 S.C. 478, 174 S.E. 461 (1934).
19. Virtue, *op. cit. supra* note 6, at 293.

Projects financed by revenue bonds are "self-supporting" in the sense that general tax funds do not subsidize and underwrite its operations. Yet to regard the revenue bond as not a debt would be a most erroneous notion. With the growing reliance of local government upon private capital any failure of the enterprise to support itself means that the taxpayers of the locality must meet the debt or else the governmental unit will suffer a significant loss in credit status.[20]

Circumventing debt limitations is only one of the reasons which the court has suggested to explain why revenue bond financing was adopted. In 1933 the State was emerging from the throes and financial difficulties of this nation's most severe depression. Taxpayers were reluctant to burden themselves further by the issuance of general obligation bonds. The procedure for issuing bonds secured by the taxing power of the State was cumbersome and time consuming and funds had to be raised quickly to take advantage of Federal grants.[21] Indeed, when one considers the immense amount of Federal subsidies for the construction of public buildings, parks, and other projects, Federal aid could very well be the most important factor producing the spectacular growth in the use of revenue bonds.

In *Luther v. Wheeler*[22] the court held that "the power to borrow money is not a necessary incident of municipal life and hence does not exist unless expressly given . . . ." Consequently, it would seem that the General Assembly must explicitly grant the power to issue revenue bonds to municipalities before this method of public financing could be utilized. Such authorization was granted by the passage of the Revenue Bond Act of 1933[23] which also granted this power to counties, townships, and other political subdivisions. With respect to the constitutionality of granting such power to political subdivisions, it is an unquestionable principle that the Legislature has unlimited powers unless limited by the Constitution. The Constitution does not prohibit the Legislature from authorizing political subdivisions to issue revenue bonds. This proposition is well-established and does not need further mention.[24]

20. For an example where a court outside South Carolina has recognized that the fate of a revenue bond is vital to the credit status of the municipality, see Philadelphia v. Fidelity-Philadelphia Trust Co., 358 Pa. 155, 160, 56 A. 2d 99, 101 (1947).

21. City of Spartanburg v. Blalock, 223 S.C. 253, 75 S.E. 2d 361 (1953).

22. 73 S.C. 83, 90, 52 S.E. 874, 876 (1905).

23. See note 16 *supra*.

24. For cases upholding the power of the General Assembly to authorize political subdivisions to issue revenue bonds, see, concerning municipalities, Cathcart v. City of Columbia, note 17 *supra;* concerning counties, Park v. Greenwood County, note 18 *supra;* concerning special authorities, Welling v.

Under the Revenue Bond Act bonds may be issued for the construction and improvement of water, sewer, light and gas systems, parking facilities, construction of public buildings, and recreational projects (such as golf courses, swimming pools and parks).[25] All bonds issued under the Act are secured solely by the revenue to be derived from the project undertaken.[26] To protect the bondholders, the borrower is required to set up and keep segregated four distinct accounts out of the gross revenues: (1) a fund for the payment of principal and interest on the bonds, (2) a fund for the expenses of operation and maintenance, (3) a fund to provide a reserve for depreciation, and (4) a "Contingent Fund" to provide a reserve for later improvements and extensions.[27] The bonds so issued constitute a lien on the system or project.[28] The unit of government involved is required to covenant that sufficient rates will be maintained to provide the necessary amounts in the respective funds mentioned above. Yet the rates may be revised as it becomes necessary.[29]

Before issuing bonds the governing body of the borrower must adopt an ordinance describing the contemplated project and the estimated cost, specifying the amount of bonds to be issued and naming the maximum rate of interest, as well as the time and place of payment.[30]

The principal and interest of revenue bonds are tax exempt under the laws of the State of South Carolina[31] and under the laws of the Federal government.[32]

As a condition of negotiability the Negotiable Instruments Law requires an instrument to contain an unconditional promise to pay a sum certain in money.[33] It further provides that the promise is not unconditional when it is made to pay out of a particular fund.[34] In light of these provisions it is well that the Revenue Bond Act ex-

Clinton-Newberry Natural Gas Authority, 221 S.C. 418, 71 S.E. 2d 7 (1952); and concerning townships, Wagner v. Johnson, 223 S.C. 471, 76 S.E. 2d 611 (1953).

25. CODE OF LAWS OF SOUTH CAROLINA, 1952 § 59-365.
26. *Id.* § 59-410.
27. *Id.* § 59-402.
28. *Id.* § 59-392; City of Spartanburg v. Blalock, 223 S.C. 253, 261, 75 S.E. 2d 361, 365 (1953).
29. CODE OF LAWS OF SOUTH CAROLINA, 1952 § 59-397.
30. *Id.* § 59-381.
31. *Id.* § 59-385.
32. INTERNAL REVENUE CODE, Sec. 103. Also, see Commissioner v. Shamberg's Estate, 144 F. 2d 998 (2d Cir. 1944), *cert. denied*, 323 U.S. 792 (1945); and Commissioner v. White's Estate, 144 F. 2d 1019 (2nd Cir. 1944), *cert. denied*, 323 U.S. 792 (1945), where the principal and interest of revenue bonds issued by state political subdivisions were held exempt from the Federal income tax.
33. CODE OF LAWS OF SOUTH CAROLINA, 1952 § 8-811.
34. *Id.* § 8-813.

plicitly provides that revenue bonds shall have all the qualities of negotiable instruments.[35]

The first question to be determined when considering the validity of revenue bonds is whether the bonds were issued for a public purpose. While the term "public purpose" can be given no precise definition, local governmental units are not limited to providing only for the absolute necessities of their citizens, but they may exercise their powers to promote the general welfare.[36]

None of the projects authorized by the Revenue Bond Act have been disapproved by the court. The more unusual enterprises held to be for a public purpose are a natural gas system,[37] a stadium,[38] and a parking lot.[39]

Property used for a public purpose may be exempt from taxation under Article X, Section 1 and Section 4 of the South Carolina Constitution. Likewise this essential feature for the exercise of governmental authority enables the power of eminent domain to be granted to the enterprise.[40]

Industrial Development Bonds

In view of the increasing industrial growth of South Carolina and the eagerness of cities and towns to attract industrial concerns, an interesting question upon which to speculate is whether a municipality in South Carolina may issue revenue bonds to finance the construction of industrial plants which will be leased to a private concern? The bonds would be secured solely by the rental from the building and land involved. What are the considerations relevant in determining the constitutionality of this plan?

Since municipal powers have always been construed strictly and are denied unless expressly granted,[41] statutory authority from the General Assembly must first be found. Assuming that a special enabling act grants the authority to the municipality to issue industrial development bonds, then, the most formidable objection would seem to be that this was not an exercise of municipal powers for a public purpose. This obstacle has been overcome in other jurisdictions, for such plans, whereby revenue bonds were to be issued for the con-

35. *Id.* § 59-384.
36. *Cf.*, Marshall v. Rose, 213 S.C. 428, 49 S.E. 2d 720 (1948).
37. Welling v. Clinton Natural Gas Authority, 221 S.C. 418, 71 S.E. 2d 7 (1952).
38. Cathcart v. City of Columbia, 170 S.C. 362, 170 S.E. 435 (1933).
39. Sammon v. City of Beaufort, 225 S.C. 490, 83 S.E. 2d 153 (1954).
40. See note 39 *supra;* McNulty v. Owens, 188 S.C. 377, 199 S.E. 425 (1938); Benjamin v. Housing Authority, 198 S.C. 79, 15 S.E. 2d 737 (1941).
41. Luther v. Wheeler, *supra* at 6.

struction of a facility to be leased to private industry in return for a rental which becomes sole security for the bonds, have been upheld by the highest court of other southern states.[42] The consensus of modern legislative and judicial thinking is to broaden the scope of activities which may be classed as involving a public purpose.[43] Economic welfare is one of the main concerns of the city, state and federal governments. This is manifested by the social security programs of both state and nation, low cost housing developments, old age insurance, and numerous other enterprises. All are illustrative of the modern concept of public purpose.

The South Carolina Constitution, Article VIII, Section 8, recognizes that the location of a manufacturing establishment is a public advantage. It states: "cities and towns may exempt from taxation by general or special ordinance, except for school purposes, manufactories established within their limits, for five successive years from the time of the establishment of such manufactories."

Opposition to the public nature of the plan could find support in *Bolton v. Wharton*[44] where the court held invalid an attempt by a city to underwrite stock in a private silk manufacturing corporation by the issuance of notes to which the taxing power of the city was pledged. In ascertaining what is a public purpose within the power to tax, such benefits as will accrue from increased taxable values and increased impetus to commercial life of the community will not suffice. Yet for two reasons this case should be inapplicable to a plan for financing a private industrial company through the issuance of revenue bonds. First, there is no pledge of the faith and credit of the issuing municipality in our proposed scheme. Secondly, the *Bolton* case really concerns a situation where a municipality attempted to issue bonds without prior statutory authority.

A path is offered, in *Haesloup v. City Council of Charleston*,[45] by which it may be found with ease that industrial development bonds are issued for a public purpose. A municipality granted land to a private person on condition that a hotel be erected thereupon. The court held that this was not a donation of public lands to private par-

42. See KY. REV. STAT. Secs. 103.200-103.280 (Cum. Supp. 1951); Faulconer v. Danville, 313 Ky. 468, 232 S.W. 2d 80 (1950).
ALA. CODE TIT. 37, Secs. 815.830 (Cum. Supp. 1951); Opinion of the Justices, 254 Ala. 506, 49 So. 2d 175 (1950); ALA. CODE TIT. 37, Secs. 511(20)-511(32) (Cum. Supp. 1951); Newberry v. Andalusia, 257 Ala. 49, 57 So. 2d 629 (1952); *In re* Opinions of the Justices, 256 Ala. 162, 53 So. 2d 840 (1951).
TENN. CODE ANN., §§ 4406.53a-4406.53n (Williams Cum. Supp. 1952); Holly v. Elizabethton, 193 Tenn. 46, 241 S.W. 2d 1001 (1951).
43. 37 AM. JUR., *Municipal Corporations* § 132.
44. 163 S. C. 242, 161 S.E. 454, 86 A.L.R. 1101 (1931).
45. 123 S.C. 272, 115 S.E. 596 (1920).

ties, but rather it was a public purpose, supported by a contractual consideration in the form of substantial returns on tax revenues. The real inquiry should be whether the proposed conveyance of real estate amounted to a breach of the trust that is imposed upon the city council "to use and dispose of the property in a way conducive to the welfare and advantage of the said city and its inhabitants."[46] In the *Haesloup* case the court indicates that when the governmental powers of taxation or of eminent domain are not authorized, the definition of a "public purpose" is broadened to include activities which may not be a "public purpose" if the powers of taxation or eminent domain have been granted.

Industrial development bonds are designed to produce further industry within a community, thereby increasing the commerce, welfare and advantages of the citizens of that area. The taxing power nor eminent domain power would be given to the private company directly aided by such bonds. Consequently, industrial development bonds should be held to be for a public purpose.

Article X, Section 6 of the South Carolina Constitution states: "The credit of the State shall not be pledged or loaned for the benefit of any individual, company, associations or corporations . . . .". This provision would not be violated since neither the taxing power nor credit of the municipality would be pledged to the obligations. The city would not be responsible for any of the debts of the corporation nor could general public funds ever be used.

Perhaps the strongest deterrent against establishing a plan for industrial development bonds is their disapproval by the investment banking world[47] and the promised uncertainty as to their future immunity from Federal taxation. This past year the United States House of Representatives approved legislation disallowing, to private businesses, rental payments made to state or local governmental units for the use of property acquired by the governmental unit by the issuance of industrial development bonds after February 8, 1954.[48] This proposed section to the Internal Revenue Code was struck by the Senate Finance Committee so that nothing ever came of the amendment.[49] Previously, the House Ways and Means Committee had discussed taxing the interest on certain municipal development

46. 123 S.C. at 283, 115 S.E. at 600.
47. The Investment Banking Association of the United States at its annual session in December, 1951, sharply condemned the issuance of bonds to finance plants for use by private manufacturing concerns. 6 NATIONAL MUNICIPAL REVIEW 319 (1952).
48. H. A. 8300, 83rd Cong., 2nd Sess. 65.
49. H. R. REP. No. 2543, 83rd Cong., 2nd Sess. 33.

bonds.[50] In 1953 the House of Representatives considered, but did not approve, a bill which would render taxable all income derived from non-general obligations of local governments issued to finance "non-public enterprises".[51] The primary advantage which industrial development bonds have is that their income is exempt from taxation. The observation is apparent that the future tax-exempt status of such bonds is in danger of being destroyed even if constitutional barriers in South Carolina were surmounted.

The questions of whether revenue bonds were issued for a public purpose and whether revenue bonds come within statutory debt limitations have been considered. Attention is now directed toward problems which are more likely to arise in the future.

Future Problems in Revenue Bond Financing

The Revenue Bond Act provides that the authorizing ordinance must create a statutory lien upon the project in favor of the bondholders. However, this lien may not be construed to give the bondholder authority to compel the sale of the project or any part thereof.[52] In *Cathcart v. City of Columbia*[53] the argument was made, that revenue bonds issued to finance a stadium were unconstitutional because the statutory lien created upon the stadium was inconsistent "with the ownership of public property and that a municipality has no power to subject its property to the possibility of its being taken over by the bondholders". The court rejected this argument saying,

> The plaintiff has cited no provision of the Constitution, and we know of none, which either forbids the Legislature to create such a lien, or denies to a municipal corporation or a county the right to so do in its exercise of the powers granted it by legislative authority.[54]

In *Sammons v. City of Beaufort*[55] revenue bonds were issued to finance on-street parking meters and an off-street parking lot. A covenant gave bondholders a lien on the "parking facilities" and provided that upon default, a receiver might be appointed to operate both the on-street and off-street parking projects. The court distinguished the *Cathcart* case from this situation and held the covenant unconstitutional. It felt that here was an attempt to create a lien

50. For additional comment, see 4 MUNICIPAL LAW SERVICE LETTER (ABA, Jan., Feb., and Sept. 1954 issues.)
51. H. R. 2734, 83rd Cong., 1st Sess. (1953).
52. CODE OF LAWS OF SOUTH CAROLINA, 1952 § 59-391.
53. 170 S.C. at 369, 170 S.E. at 437.
54. *Id.* at 369, 170 S.W. at 438.
55. 225 S.C. 490, 83 S.E. 2d 153 (1954).

upon "on-street parking facilities, *an essential governmental function*". However, objections to the lien were not fully stated. "It would hardly be suggested that a municipality may mortgage its streets or delegate to a court the power to regulate traffic. This covenant is obviously invalid so far as it pertains to on-street parking facilities."[56]

Apparently, if the project financed by revenue bonds is considered an "essential governmental function", then the statutory lien authorized by the Revenue Bond Act is invalid. As it is generally agreed that the answerability of the property protects the investor,[57] the marketing of a revenue bond without this lien would probably be unsuccessful. However, thus far there is no indication outside of the *Sammons* case as to which projects authorized by the Revenue Bond Act can be considered an "essential governmental function".

In the *Sammons* case perhaps the greater difficulty lay with the covenant under which a receiver would have power not only to operate facilities and collect revenues but also to determine rates and charges on the police power theory of on-street parking meters. The court possibly felt that to enable a judicial officer to fix parking meter charges on that basis is to entrust him with the police power. If the court was more concerned with the power of a receiver upon default of the bonds, than with the power of bondholders under the statutory lien to compel the performance of all duties of the officials of the borrower as well as other rights given to the bondholders, then the receivership problem may be eliminated by restricting the duties of a receiver to routine administration and collection of revenues.[58]

Revenue bonds are frequently used as a method of financing parking facilities. Such projects are constitutional under the police power of the local governmental unit. However, the police power may not be used for general revenue purposes.[59] In *Owens v. Owens, Mayor*,[60] revenue bonds were secured by the pledge of proceeds from on-street parking meters. The court rejected the argument of the plaintiff that the purpose of the city was to raise revenue under the guise of a police regulation. Insufficient facts were established to show that revenue collected from the parking meters exceeded the cost of this method of regulating traffic and the use of the streets. The court held that "the city should be allowed to make a charge

56. *Id.* at 158.
57. See note 6 *supra*.
58. 4 MUNICIPAL LAW SERVICE LETTER, Sept. 1954, page 3.
59. Owens v. Owens, Mayor, 193 S.C. 260, 8 S.E. 2d 339 (1940); Sammons v. City of Beaufort, 225 S.C. 490, 83 S.E. 2d 153 (1954); 25 AM. JUR., *Highways* §§ 182, 184.
60. 193 S.C. 260, 8 S.E. 2d 339 (1940).

large enough to cover the expense which may reasonably be expected".[61] In the *Sammons* case a municipality was held to be validly exercising its police power by using revenue from on-street parking meters to defray the cost of off-street parking facilities. Also, the municipality was allowed to create a financial "cushion" for the payment of the revenue bonds if the revenue collected was in excess of the immediate expense.

One inference to be drawn from the *Owens* and *Sammons* cases is that the court must give its approval upon whether revenue received under an exercise of the police power constitutes a reasonable charge in relation to the expense of the activity. In some respects the attitude of the court is similar to its position toward Special Fund Bonds where it determines the sufficiency of the fund created to support the bonds.[62]

The local governing body may not covenant to make it a crime for a person to use the services provided by the revenue bond project without payment of the established charge and to covenant further to keep the sanction in effect during the life of the bonds. In the *Sammons* case, where there was this type of covenant, the court indicated this view by saying, "No city council may be empowered to enact any kind of criminal ordinance and make same irrevocable."[63] No reasons were given for this holding. The views of the highest court in a sister State, North Carolina, are not helpful even though the result is substantially the same. In *Britt v. City of Wilmington*[64] a penalty provision was held invalid on the ground that a regulation as to a purely proprietary activity may not be enforced by criminal prosecution. However, South Carolina recognizes no distinction between governmental and proprietary activity[65] and this latter holding in the *Sammons* case remains unexplainable as to why punitive sanctions may not be employed to protect public property in its proper use.

The true type of revenue producing facility is a project or system operated by the body issuing the bonds, and charges are made against members of the public to whom the services are furnished. Such projects are sometimes described as "self-liquidating".[66] This classification would include such facilities as water, electric, and gas systems, bridges, toll roads, ferries, hospitals, and athletic stadiums.

61. 193 S.C. at 266, 8 S.E. 2d at 341.
62. See Arthur v. Byrnes, note 12 *supra.*
63. 83 S.E. 2d at 158.
64. 236 N.C. 446, 73 S.E. 2d 289 (1952).
65. Irvine v. Town of Greenwood, 89 S.C. 511, 72 S.E. 228 (1911); Farrow v. City of Columbia, 169 S.C. 373, 168 S.E. 852 (1933); Looper v. City of Easley, 172 S.C. 11, 172 S.E. 705 (1934).
66. See Rose, note 2 *supra* at 394.

However, the Revenue Bond Act specifically authorizes bonds to be issued for the acquisition of facilities such as city halls, courthouses, fire stations and other public buildings.[67] These facilities do not produce income from the public for the rendition of a particular service. South Carolina case law concerning this latter type of public project is very scant.

One method of financing the non-revenue type facility would be to create two public bodies; one to acquire and own the facility and to issue revenue bonds for that purpose, payable out of rentals due to be paid by the other public body under a lease of the facility. The lease would run for the life of the bonds, and the amount of rent contracted to be paid would cover operational expenses and debt service requirements on the bonds. The lessee pays the rentals out of tax moneys or other revenues not derived from the operation of the facility.

In *Bollin v. Graydon*[68] there was a plan of financing a courthouse which was very similar to the one outlined in the preceding paragraph. A courthouse building commission was created by the General Assembly[69] with authority to construct a courthouse for the purpose of conducting public business of the county. Each county officer was to maintain offices in the building where business pertaining to the office was to be conducted. Fees were to be collected for certain functions performed by the officers. The fees were to be turned over to the treasury of the county as general county revenues and would constitute a fund securing revenue bonds issued to finance the building. A contract was then signed between the building commission and a county board of commissioners under which the courthouse was leased to the latter for the term of the life of the bonds at an annual rental estimated to be sufficient to retire them. The court held that each board of commissioners was a separate corporate body which had the power to enter into the rental agreement, and that the pledging of fees was not an attempt to delegate to the bondholders power to exercise the taxing power of the county.

The court in the *Bollin* case did not discuss the following problem which may arise later in a similar situation. Even if the bonds themselves are not a public debt, an argument may be made that the lease constituted a debt of the lessee, within the meaning of constitutional debt limitations, for the aggregate of all rentals provided for in the lease. Courts of other jurisdictions have held that long term leases

67. CODE OF LAWS OF SOUTH CAROLINA, 1952 § 59-365.
68. 177 S.C. 374, 181 S.E. 467 (1935).
69. 39 ST. AT LARGE 1089, Act June 5, 1935.

of this nature are debts only to the extent that the subject matter of the contract has been furnished by one of the parties. In other words a distinction is drawn between an absolute debt created at once and so-called "future indebtedness".[70] This latter rule is known as the "Walla-Walla Doctrine".[71] It was enunciated in a case involving a municipal contract for a supply of water running over a period of years payable in annual installments. Whether the lessee acquires title at the expiration of the lease is another factor which has frequently been deemed crucial.[72] In view of the tendency of the court to find debt obligations not within the constitutional meaning of debt, probably the "Walla-Walla Doctrine" would be applied.

If the court refuses to accept the "Walla-Walla Doctrine", then non-revenue facilities can be financed by a lease for a short period, perhaps one or two years, with periodic options of renewal granted to the lessee continuing over the entire maturity of the bonds issued to finance the facility.[73] Many issues of revenue bonds made payable solely from the proceeds of one of these short-term leases have been marketed advantageously.[74]

An alternative method of financing non-revenue producing facilities would be to carry the lease plan one step further. Instead of having two public bodies, as in the conventional lease plan, the municipality or other unit could retain title to the facility and issue its own securities for the acquisition thereof, payable out of so-called revenues from the facility, and then covenant to provide those revenues by making periodic payments from other sources payable into a special fund created to service the bonds. The payments into the special fund would be called "rents" and should be equal to the reasonable value of the use of the facility. While in essence this plan means that the issuing body is making payments called "rents" for the use of a facility owned by it, the scheme would seem to amount only to the traditional Special Fund Bond without the pledge of the full faith, credit and taxing power of the issuing body. Only the project itself and the revenues from the use thereof would be answerable to the bondholder.[75]

Many states do not permit the pledge of revenues from sources other than income which can be directly traced to the particular pro-

70. See Rose, note 2 *supra* at 395.
71. Walla Walla v. Walla Walla Water Co., 172 U.S. 1 (1898).
72. Farguhar v. McAlevy, 142 Pa. 233, 21 Atl. 811 (1891).
73. *E. g.*, Opinion of the Justices, 147 Me. 410, 79 A. 2d 753 (1951).
74. Rose, note 2 *supra* at 396.
75. For an example of this plan of financing, see Martin County v. Cassady, 307 Ky. 728, 212 S.W. 2d 281 (1948).

ject which was financed by revenue bonds.[76] However, the South Carolina court has adopted a slightly different view on this point. One of the projects to be financed by revenue bonds, in *Cathcart v. Columbia,* was an enlargement of a city water works system. The bonds were to be secured by a pledge not only of revenues from additions to the waterworks system, but also the present revenues of the water department. The plaintiff contended that the effect of the loan would be that the city would be required to replace such revenues by taxation and therefore the loan would be a debt within the meaning of the Constitution. The court rejected this argument[77] without stating reasons of its own, but relied upon the language of an Illinois decision, *Ward v. City of Chicago.*[78] In that case, certificates of indebtedness payable solely from revenues derived from the city's waterworks system, even though the debts were created to finance the enlargement of a plant, were held not to constitute a debt within constitutional limitations. By relying upon the *Ward* case the court would seem to have given its approval to a revenue bond being "sweetened" by a pledge of revenues derived from a source other than the project itself.

Conclusion

The Special Fund Doctrine in South Carolina has mitigated constitutional debt limitations, but its dangers have been eased by the court's holding that the determination of the special fund is a judicial function. Revenue bonds constitute the final ramification of the Special Fund Doctrine. It is well-established that revenue bonds are not a debt within the meaning of constitutional debt limitations. One may also conclude, with a substantial degree of certainty, that projects authorized by the Revenue Bond Act in South Carolina are valid public purposes.

Industrial development bonds, if and when issued, would probably be constitutional, but the future of their tax exempt status should be a primary factor in their consideration.

Some uncertainty exists with respect to the validity of the statutory lien given to bondholders, particularly if the project acquired comes within the classification of an "essential governmental function".

76. See, *e. g.,* Opp v. Donaldson, 230 Ala. 189, 163 So. 232 (1935); State *ex rel.* Public Institutional Bldg. Authority v. Griffith, 135 Ohio St. 604, 22 N.E. 2d 200 (1939); *Contra:* Schmeller v. Ft. Lauderdale, 38 So. 2d 36 (Fla. 1948).
77. 170 S.C. at 372, 170 S.E. at 439.
78. 342 Ill. 167, 172, 173 N.E. 810, 812 (1930).

The financing of non-revenue producing facilities has aroused little concern thus far, but various plans by which such projects can be financed should be constitutional.

The courts would also seem to approve of the financing of the extension of existing facilities by the pledging of funds derived from the existing facilities as well as the extension itself.

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