

February 9, 2009

Muddying the Water: General Obligation Bonds

The words, general obligation bonds, have a specific meaning for those of us in the municipal bond business. Those words mean that the bonds are backed by the full faith and credit and taxing power of a municipality, including that the bonds are backed by ad valorem property taxes.

On February 9, 2009, Rutgers University issued bonds based on the revenue of Rutgers University as a negotiated issue through Morgan Stanley. For some reason, they called them "General Obligation Bonds." This is very misleading.

In the Preliminary Offering Statement for this issue under the heading of "Security for the Bonds," it states that

The Indenture provides that the 2009 Series F Bonds shall be direct and general obligations of the University, and that the full faith and credit of the University shall be pledged for the payment of the principal and Redemption Price thereof and interest thereon; provided, however, there shall be excluded from the pledge of the Indenture any revenues, moneys, securities or funds heretofore or hereafter specially pledged by the University for the payment of other bonds, notes or other indebtedness. (p. 5)

In other words, these are revenue bond, bonds backed by the revenue of the University. They may be very fine bonds, but there are not general obligation bonds in the way that term has been used in the municipal bond market, and therefore it is very misleading.