



State Issued Appropriation Bonds

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At a Glance

- The state has authorized state appropriation bonds to fund the following:
 - 1) a Pay-for-Performance program (2011);
 - 2) refunding tobacco settlement revenue bonds that were sold to close a budget gap (2011) and to refinance those bonds (2022);
 - 3) construction of the Vikings stadium (2012);
 - 4) construction of the Lewis and Clark water project in Southwest Minnesota (2015 and 2017);
 - 5) specified projects to protect, conserve, preserve, and enhance the state’s air, water, land, fish, wildlife, and other natural resources (2018), later repealed;
 - 6) public infrastructure projects in the city of Duluth (2019);
 - 7) electric vehicle infrastructure on state property (2020);
 - 8) equipment grants to public television stations (2020); and
 - 9) remedial actions at several contaminated sites (2020).
- A bill authorizing appropriation bonds does not require a 3/5 vote to pass; a majority is enough.
- Appropriation bonds proceeds can be used in ways that general obligation bond proceeds cannot, such as to improve private property and on non-capital expenditures.
- Appropriation bonds count toward the debt limit suggested by the state’s capital investment guidelines (Guidelines 1 and 2, but not Guideline 3).
- Appropriation bonds are not backed by the state’s promise to tax to repay them like general obligation bonds are. This makes them a higher risk investment, for which the state likely must pay a higher interest rate than for general obligation bonds.

What is an appropriation bond?

An appropriation bond is one of many kinds of debt financing instruments the state can sell to raise a relatively large sum of money from investors in the short term in exchange for a promise to repay the debt in smaller increments over time with interest.

Bonds are named based on the commitment the state makes to bond holders about how the state will make payments on the bonds. “Appropriation” bonds are so named because the money used to make payments on the debt comes from an appropriation passed in law by the legislature; the state makes no promise to make payments on the bonds in the absence of such an appropriation. In contrast, “general obligation” bonds are backed by the full faith, credit, and taxing authority of the state; the state promises to raise taxes, if need be, to make payments on general obligation bonds. “Revenue”

bonds are backed by a specific, identified source of revenue; the state makes no promise to make payments on the debt beyond the money available from the specified revenue source.

How do appropriation bonds work? What promise does the state make to pay back appropriation bonds?

When the state sells appropriation bonds, the state promises bond purchasers that the state will make payments on the bonds only if the legislature appropriates money for that purpose. This is described clearly in the “official statement,” the document that expresses the terms of the contract between the state and the bond purchasers:

[These appropriation] bonds are payable in each fiscal year only from amounts appropriated by the legislature of the state pursuant to the act and according to the terms of the order for the payment of the bonds. No other revenues or assets of the state...are pledged for the payment of the principal of or interest on the bonds. The bonds are not public debt of the state subject to constitutional limitations on indebtedness, and the full faith, credit, and taxing powers of the state are not pledged to the payment of the bonds or to any payment that the state agrees to make under the act and the order. The bonds are not payable directly, in whole or in part, from a tax of statewide application on any class of property, income, transaction, or privilege.¹

Further, the state may reduce or repeal an appropriation or fail to pass an appropriation, and therefore stop making payments on the bonds, and the bond holder will have no legal recourse against the state:

The bonds shall be cancelled and shall no longer be outstanding on the first day of a fiscal year for which the legislature shall not have appropriated amounts sufficient for payment of principal of and interest on the bonds. Amounts appropriated to pay principal of and interest on the bonds constitute a continuing appropriation that does not require any further action by the legislature; however, continuing appropriations may be reduced or repealed in their entirety by the legislature. State appropriations, including continuing appropriations, are also subject to executive unallotment, in whole or in part, under Minnesota Statutes, section 16A.152.²

Because of these contractual limits on the state’s legal obligation to make payments, appropriation bonds are inherently riskier for bond holders than general obligation bonds that are backed by a state constitutional requirement to raise taxes to make payments. Therefore, bond purchasers will likely demand a higher interest rate on appropriation bonds than on general obligation bonds, assuming market conditions and other factors that affect interest rates are equal.

Though the legal obligation to repay appropriation bonds is limited, the state likely would face other undesirable consequences for non-appropriation. Credit rating agencies likely would downgrade the state’s credit rating. The securities marketplace would view the state’s credit-worthiness with skepticism, making future borrowing expensive or perhaps even impossible.

¹ [“Official Statement, State of Minnesota, State General Fund Appropriation Refunding Bonds,”](#) November 2012, p. 6. A similar statement is contained in the Official Statements for each of the state’s issuances of appropriation bonds.

² [“Official Statement, State of Minnesota, State General Fund Appropriation Refunding Bonds,”](#) November 2012, p. 7.

Can legislation that authorizes appropriation bonds pass with a majority vote?

Yes. The legislature likely can pass a bill that authorizes appropriation bonds with a majority. This contrasts with a bill authorizing general obligation bonds that requires a vote of 3/5 of each body to pass, if the bonds are used to improve land and buildings.³ (General obligation bonds for certain items other than land and building improvements can be authorized with a majority vote.⁴)

Must a bill that authorizes appropriation bonds originate in the House?

Likely, no. Because appropriation bonds are not backed by the taxing powers of the state, a bill to authorize their sale is not likely to be deemed a bill that “raises revenue.” Therefore, it is likely not necessary for such a bill to originate in the house of representatives.

What can appropriation bonds be used for?

Like all state money, money raised by sale of appropriation bonds must be spent for a public purpose. Beyond that, there are no constitutional or statutory limits on what the state can pay for with money raised by the sale of appropriation bonds. This is another important feature that distinguishes appropriation bonds from general obligation bonds. General obligation bonds for land and building improvements can only be used for property that is publicly owned.

Do appropriation bonds count toward limits on capital investment guidelines?

The commissioner of management and budget has issued guidelines to limit the amount of debt the state carries. Debt financed with appropriation bonds counts toward those limits.

Comparison of Appropriation Bonds to General Obligation Bonds

The following table sums up the major distinctions between appropriation bonds and general obligation bonds, described in earlier paragraphs.

³ Minnesota Constitution. article XI, section 5.

⁴ Minnesota Constitution. article XI, section 5.

COMPARISON of APPROPRIATION BONDS to G.O. BONDS

	General Obligation Bonds	Appropriation Bonds
Vote required for passage	3/5 (for improvements to land/buildings)	Majority
Count toward debt guidelines?	Yes	Yes
Backed by requirement to tax to pay debt service?	Yes	No
What can be funded with them?	Only things that fall within categories listed in the Constitution. For land and buildings, improvements must be publicly owned and capital in nature. Must be for a public purpose, as required for all expenditures of state funds.	Must be for a public purpose, as required for all expenditures of state funds.
Must a bill originate in the House?	Probably, because the bill arguably raises revenue due to the constitutional requirement to tax to repay them.	No
Source of repayment on the bonds	General fund transfer to the state bond fund of the amount needed to pay principal and interest. Minn. Stat. section 16A.641, subd. 10.	As appropriated in session law or by statute, specific to the authorized project.
Security	Backed by a constitutional requirement to tax to make payments.	Bond holders have no legal recourse if the state does not appropriate money to pay the bonds.

When and for what purposes has the state used appropriation bonds?

In 2011, the state authorized appropriation bonds for the first time to fund a pay-for-performance program.⁵ Proceeds from the sale of appropriation bonds were to be used to pay service providers for meeting performance and outcomes as specified by an oversight committee.⁶ No bonds have been issued to fund this program.

Also in 2011, the state authorized, and in 2012 sold, revenue bonds backed by payments the state was receiving from a settlement in 1998 of a lawsuit brought by the state against certain tobacco companies for liability for health consequences of smoking that had been borne by the state.⁷ This money was used to close a budget gap. The 2011 law⁸ authorized the state to sell appropriation bonds to refund the tobacco settlement revenue bonds, because appropriation bonds were expected to carry a lower interest rate than the revenue bonds. These appropriation bonds were sold in two series: Series 2012A taxable bonds for \$54,665,000 and Series 2012B tax-exempt bonds for \$601,555,000, for a total of \$656,220,000.

⁵ Laws of Minnesota 2011, 1st Spec. Sess., chapter 10, article 3, section 28.

⁶ Minnesota Statutes 2016, sections 16A.93-16A.96.

⁷ [State of Minnesota and Blue Cross Blue Shield of Minnesota vs. Phillip Morris, et al, Civil Case No. C1-94-8565, settled](#) in 1998).

⁸ Laws of Minnesota 2011, 1st Spec. Sess., chapter 7, article 11, section 4.

In 2012, the state authorized the sale of appropriation bonds to pay for a portion of the construction of a professional football stadium.⁹ These bonds were sold in 2014 in two series: Series 2014A tax-exempt bonds for \$391,785,000 and Series 2014B taxable bonds for \$70,280,000, for a total of \$462,065,000.

In the Omnibus Bonding Bill of 2015,¹⁰ the state authorized the sale of \$19,000,000 in appropriation bonds to pay for a segment of the Lewis and Clark Regional Water System Project, to deliver water from an aquifer in South Dakota to communities in southwest Minnesota. Specifically, this appropriation was for completion of the pipeline to Magnolia, Minnesota, extension of the project to the Lincoln Pipestone Rural Water System connection near Adrian, Minnesota, and engineering, design, and easement acquisition for the final phase of the project to Worthington, Minnesota.¹¹

In the Omnibus Bonding Bill of 2017,¹² the state authorized the sale of \$3,500,000 in appropriation bonds to finance Phase 3 of the Lewis and Clark Regional Water System Project. Phase 3 of the project included extending the project from the Lincoln-Pipestone Rural Water System connection near Adrian to Worthington, constructing a reservoir in Nobles County and a meter building in Worthington, and acquisition and installation of a supervisory control and data acquisition system.¹³

In the Omnibus Bonding Bill of 2018,¹⁴ the state authorized the sale of \$98,000,000 in appropriation bonds to be repaid using money deposited in the Environmental and Natural Resources Trust Fund (ENRTF). Under the Constitution, money from the sale of lottery tickets is deposited into the ENRTF and is dedicated to specified purposes. Due to a legal challenge, these bonds were not sold, and the authorization was repealed in 2019.¹⁵

In the Omnibus Tax Bill of 2019,¹⁶ the state authorized the sale of \$97,720,000 in appropriation bonds for public infrastructure projects in the city of Duluth.

In the Omnibus Bonding Bill of 2020,¹⁷ the state authorized the sale of appropriation bonds for three purposes:

1. Electric vehicle infrastructure on state-owned property: \$2,000,000
2. Public television equipment grants: \$15,000,000
3. Removal and remedial actions to address risks to human health and the environment at contaminated sites, including the Duluth Dump #1 Superfund site; Esko Groundwater Contamination site; the Perham Arsenic site; and the Precision Plating State Superfund site in Minneapolis: \$30,400,000

In October 2022, the commissioner of management and budget sold appropriation bonds to refund a portion of the tax exempt appropriation bonds sold in 2012 to close the budget gap.

⁹ Laws of Minnesota 2012, chapter 299, article 2, section 1; amended in Laws of Minnesota 2013, chapter 125, article 1, section 11.

¹⁰ Laws of Minnesota 2015, 1st Spec. Sess., chapter 5.

¹¹ Laws of Minnesota 2015, 1st Spec. Sess., chapter 5, article 3, section 1, subdivision 2.

¹² Laws of Minnesota 2017, 1st Spec. Sess., chapter 8.

¹³ Laws of Minnesota 2017, 1st Spec. Sess., chapter 8, article 2, section 2, subdivision 2b.

¹⁴ Laws of Minnesota 2018, chapter 214, article 6.

¹⁵ Laws of Minnesota 2019, chapter 2, article 1, section 9.

¹⁶ Laws of Minnesota 2019, 1st Spec. Sess., chapter 6, article 10.

¹⁷ Laws of Minnesota 2020, 5th Spec. Sess., ch 3, article 4.

The following table summarizes all issuances of appropriation bonds under the authorizations discussed above.

Issuances of Appropriation Bonds

	Authorized	Issued	Amount Issued
Pay for Performance Program	Laws 2011, 1st Spec. Sess., ch. 10, art. 3, s 28.	Not issued	--
Budget gap - Refunding tobacco settlement revenue bonds	16A.99 (Laws 2011, 1st Spec. Sess., ch. 7, art. 11, sec. 4.)	November 2012	\$656,220,000 – TOTAL \$54,665,000 – Taxable; \$601,555,000 – Tax exempt
Professional football stadium construction	16A.965 (Laws 2012, ch 299, art. 2, sec. 1; amended in Laws 2013, ch. 125, art. 1 sec. 11) – Repealed 2023.	January 2014	\$462,065,000 - TOTAL \$70,280,000 – Taxable; \$391,785,000 – Tax exempt
Lewis and Clark water system project	16A.967 (Laws 2015, 1st Spec. Sess., ch. 5; amended in Laws 2017, 1 st Spec. Sess, ch. 8.)	October 2016	\$11,790,000 – TOTAL, all taxable
Lewis and Clark water system project	16A.967 (Laws 2017, 1 st Spec. Sess., ch. 8)	November 2017	\$7,570,000 – TOTAL, all taxable
Environment and Natural Resources projects	Laws 2018, ch. 214, art. 6. Repealed by Laws 2019, ch. 2, art. 1, sec. 9.	Repealed	--
Duluth Regional Exchange District	16A.968 (Laws 2019, 1 st Spec. Sess., ch. 6, art. 10, s. 1 (\$97,720,000 authorized))	November 2020 October 2021 October 2023	\$66,300,000 – all taxable \$6,920,000 – all taxable \$26,080,000 – all taxable
Electric vehicle infrastructure on state-owned property	16A.963 (Laws 2020, 5 th Spec. Sess., ch. 3, art. 4, s. 1 (\$2,000,000 authorized))	October 2021	\$1,875,000 – all taxable
Public television equipment grants	16A.964 (Laws 2020, 5 th Spec. Sess., ch 3, art. 4, s. 2 (\$15,000,000 authorized))	October 2021	\$14,050,000 – all taxable
Environmental cleanup at specified sites	16A.966 (Laws 2020, 5 th Spec. Sess., ch 3, art. 4, s. 3 (\$30,400,000 authorized))	October 2021	\$29,670,000 – all taxable
Refinancing 2012 appropriation bonds	16A.99 (Commissioner’s authority to refinance outstanding bonds)	October 2022	\$338,300,000 – tax exempt

Does the constitution permit the state to sell appropriation bonds?

Appropriation bonds were a new debt instrument for the state when the state first sold them in 2012. Because they were new, and because the Minnesota constitution¹⁸ restricts use of “public debt,” there was some uncertainty as to the legal status of these new appropriation bonds. Would they be

¹⁸ Minnesota Constitution. article XI, section 5.

interpreted to be “public debt” like general obligation bonds and therefore subject to the same constitutional restrictions, such as public ownership, limits on acceptable purposes, and requiring a 3/5 vote if used for improvements to land and buildings? Could proceeds from appropriation bonds be used to plug a budget hole, even though the constitution requires a balanced budget?

These questions had been considered in 2009, when then-governor Tim Pawlenty proposed appropriation bonds as a component of the 2010-2011 biennial budget. The Attorney General expressed skepticism:

In response to an inquiry from then-Senate Majority Leader Larry Pogemiller, Attorney General Lori Swanson analyzed the constitutionality of the proposed bonds and observed that the State would essentially be borrowing money to balance its budget. Noting that the Minnesota Constitution limits the purposes for which public debt may be incurred, the Attorney General was ‘not confident’ that a court would uphold the constitutionality of the bonds in light of ‘the balanced budget requirement in the Minnesota Constitution.’¹⁹

That legislature did not authorize the sale of appropriation bonds that year.

When the next legislature faced a significant challenge to balancing the budget in 2011 for the biennium 2012-2013, Governor Dayton and the legislature turned again to the tobacco settlement revenue and appropriation bonds. The budget bills passed in the summer of 2011, after a three-week government shutdown, provided for issuing revenue bonds to be repaid with tobacco settlement money. Those revenue bonds were to be refinanced, essentially, by issuing appropriation bonds to refund the tobacco revenue bonds. At the time, the commissioner of management and budget estimated that this refinancing would save the state about \$65.5 million, due to a lower interest rate on appropriation bonds.²⁰

The 2011 law that authorized appropriation bonds to refund tobacco settlement revenue bonds established a validation procedure by which the Minnesota Supreme Court would be asked to clarify the legal status of appropriation bonds. The validation procedure provided for the commissioner of management and budget to bring a lawsuit against the state, to be decided by the Minnesota Supreme Court. Accordingly, then-commissioner James Schowalter filed a complaint with the court on April 5, 2012 to begin the suit.

Before the Supreme Court issued an order in the case, the legislature passed a bill to pay for construction of a professional football stadium for the Vikings using appropriation bonds.

The Minnesota Supreme Court heard oral arguments in late August 2012. Alan Gilbert from the Attorney General’s office argued on behalf of the state that appropriation bonds constituted “a subterfuge to evade the balanced budget requirement” of the Minnesota Constitution and were “public debt” subject to the same constitutional constraints as general obligation bonds.²¹ Attorneys from Kutak Rock, LLP, argued on behalf of the commissioner of management and budget that appropriation bonds were not public debt and therefore not subject to those constitutional constraints.

¹⁹ [James D. Schowalter, in his capacity as Commissioner of the Minnesota Department of Management and Budget v. The State of Minnesota and the Taxpayers and Citizens of the State of Minnesota](#), 822 N.W.2d. 292, 295 (Minn. 2012).

²⁰ [Schowalter v. Minnesota](#), 822 N.W.2d 292, 296 (Minn. 2012).

²¹ [Schowalter v. Minnesota](#), 822 N.W.2d 292, 294 (Minn. 2012).

On October 31, 2012, the Minnesota Supreme Court rendered its decision: appropriation bonds are not “public debt.”²² “Public debt” by definition means debt that is backed by the full faith, credit and taxing powers of the state. A debt that is not backed by that promise is not “public debt” and therefore isn’t constrained in the same way as public debt. The court relied heavily on the representations, and lack of warranty, in the Official Statement, quoted above, to determine that the tobacco settlement refunding appropriation bonds were not backed by the state’s full faith, credit, and taxing authority. Therefore, appropriation bonds are not public debt.

This decision cleared the way for the state’s first sale of state-issued appropriation bonds in November 2012. Subsequent sales of appropriation bonds have included essentially the same disclaimer language in their Official Statements and have relied upon the same Supreme Court decision in the Schowalter case as to their validity.

How are state-issued appropriation bonds similar to other debt financing instruments used by the state and its agencies?

The state and its agencies have entered into a variety of financing arrangements that are conceptually similar to state-issued appropriation bonds in the sense that the state or agency makes payments from appropriations from the state’s general fund. These other arrangements include lease-purchase agreements, real estate leases, certificates of participation, and bonds issued by the University of Minnesota and other agencies. One example of agency-issued appropriation bonds are housing infrastructure bonds issued by the Minnesota Housing Finance Agency. Under agreements reflecting these arrangements, the state’s or agency’s obligation to make payments is subject to an appropriation of money; if no appropriation is made (or is insufficient, repealed or unallotted), then the other party in the agreement has no legal recourse. The state debt capacity forecast lists these financing arrangements for which principal is outstanding, and accounts for them in determining the state’s debt capacity under capital investment Guidelines 1 and 2, but not Guideline 3, established by the commissioner of management and budget.

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²² [Schowalter v. Minnesota](#), 822 N.W.2d. 292 (Minn. 2012).