MEMORANDUM

To: Banking Committee

From: Board Office

Subject: Sale and Award of $8,465,000 Academic Building Revenue Refunding Bonds, Series U.N.I. 2003

Date: March 31, 2003

Recommended Action:

Recommend that the Board adopt the following resolutions (see G.D. 8), subject to receipt of acceptable bids:

1. A Resolution providing for the sale and award of $8,465,000 Academic Building Revenue Refunding Bonds, Series. U.N.I. 2003, and approving and authorizing the agreement of such sale and award.

2. A Resolution authorizing and providing for the issuance and securing the payment of $8,465,000 Academic Building Revenue Refunding Bonds, Series U.N.I. 2003, for the purpose of refunding the 2005 through 2015 maturities of the $3,900,000 Academic Building Revenue Bonds, Series U.N.I. 1992, dated June 1, 1992, and the 2005 through 2015 maturities of the $7,440,000 Academic Building Revenue Bonds, Series U.N.I. 1993, dated July 1, 1993, presently outstanding and heretofore issued by the Board to defray costs of building construction projects on the campus of the University of Northern Iowa.

Executive Summary:

The Banking Committee is requested to recommend that the Board adopt two resolutions related to the sale, award and issuance of $8,465,000 Academic Building Revenue Refunding Bonds, Series U.N.I. 2003.

At its March 2003 meeting, the Board authorized the Executive Director to fix the date(s) for the sale of the bonds, which would be sold to refund outstanding maturities of the U.N.I. Academic Building Revenue Bonds, Series 1992 and Series 1993.

The proposed refunding would be a current refunding, as the call date for the outstanding bonds is July 1, 2003.

Pursuant to §229 of House File 2627 of the 2002 General Assembly, the refunding needs to be done in coordination with the Tobacco Settlement Authority. Correspondence was sent to the Tobacco Settlement Authority requesting necessary approvals; authorization to proceed with the refunding was received.

However, Treasurer Fitzgerald, as Chair of the Tobacco Settlement Authority, expressed concerns about the timing of the refunding and FY 2004 appropriations; therefore, the 2004 maturities are excluded from the refunding.

Tuition and fee revenues are used for debt service payments on Academic Building Revenue Bonds; a tuition replacement appropriation replaces that university revenue.

The estimated net future value and net present value savings from the refunding in future tuition replacement appropriations between 2005 and 2015 total approximately $900,000 and $700,000, respectively.

The maturity schedules for the bonds would not change with the refunding.

Interest on the refunding bonds would be exempt from federal and state taxes (double tax-exempt) for individuals who are Iowa residents and purchase the bonds. Interest on the bonds to be refunded has also been double tax-exempt.

Background:

Interest Rates

Bond coupon rates and the net interest rate for Regent bonds are very dependent upon market conditions at the time of issuance.

The net interest rate for Academic Building Revenue Bonds (including refunding bonds) issued since 1971 has ranged from a low of 4.32% in 2002 to a high of 11.19% in 1981.

As interest rates decline, bonds can be refunded and annual and total debt service costs reduced. In the case of Academic Building Revenue Bonds, reduced annual debt service reduces the amount needed from the tuition replacement appropriation.

Tuition Replacement Appropriations

Tuition replacement appropriations represent an ongoing commitment of the state to meet the debt service cost of Academic Building Revenue Bonds. Tuition and fee revenues are pledged for debt service payments for the bonds and the tuition replacement appropriation replaces that university revenue.

Tuition replacement needs for each university are comprised of debt service payments (principal and interest), less the net interest earned on the sinking and reserve funds. As reserve funds are reinvested at interest rates lower than currently being earned, interest earnings will decline and the amount needed for the tuition replacement appropriation will increase, absent any refundings.

Tobacco Bond Proceeds

The Board Office advised the Board in June 2002, that language was included in HF 2627 (2002 session) that restricted the refunding of outstanding debt service that is scheduled to be paid from tobacco bond proceeds.

The July 1, 2003 – July 1, 2007 principal payments for the bond issues for which refunding is proposed are scheduled to be paid from tobacco bond proceeds.

Late in the summer of 2002, the Board Office received a copy of a letter sent to Treasurer of State Michael Fitzgerald as Chair of the Tobacco Settlement Authority from Mr. Robert Helmick of the Dorsey Law Firm, who serves as tax counsel to the Tobacco Settlement Authority.

In the letter Mr. Helmick indicates that the Board of Regents can continue to effect savings in interest costs and reduce tuition replacement appropriations in the future if the refunding is done in coordination with the Tobacco Settlement Authority so that proper amendments to the Tobacco Settlement Financing Plan and tax certificate can be made.

In a February 25, 2003 letter, Executive Director Nichols requested necessary approvals from Treasurer Fitzgerald by March 14, 2003 if the Board were to proceed with the refunding at its April 2003 meeting.

On March 14, 2003, Executive Director Nichols received a letter from Treasurer Fitzgerald authorizing the refunding, although concerns were raised about the timing of the refunding and FY 2004 appropriations for tuition replacement. As a result of these concerns, the 2004 maturities have been excluded from the refunding. Excluding the 2004 maturities does not significantly reduce the savings from the refunding.

Definition of Refunding

A refunding is the issuance of bonds whose proceeds are used to pay principal, interest and/or call premium, if any, of an existing debt obligation; the old (refunded) debt is replaced with new (refunding) bonds.

<u>Analysis</u>:

Bonds to be Refunded

The proceeds from the sale of the proposed refunding bonds would be used to refund bond principal of the Board's Academic Building Revenue Bonds, Series U.N.I. 1992 and Series U.N.I. 1993. The principal to be refunded for the two bond issues totals $8,430,000. There is no call premium.

The 1992 bonds were issued in the amount of $3,900,000, with a net interest rate of 5.91%, for fire and environmental safety, deferred maintenance, equipment and utility projects at the University of Northern Iowa.

- The coupon (interest) rates on the 2005 – 2015 maturities (total principal amount of $3,120,000) of the 1992 bonds range from 5.5% in 2005 to 6.0% in 2015.

- The present value savings from the refunding of the 1992 bonds is estimated at slightly more than $400,000.

The 1993 bonds were issued in the amount of $7,440,000, with a net interest rate of 4.82%, for construction of an additional floor and improvements to the Rod Library at the University of Northern Iowa.

- Coupon rates on the 2005 – 2015 maturities (total principal amount of $5,310,000) of the 1993 bonds range from 4.5% in 2005 to 5.0% in 2015.
- The present value savings from the refunding of the 1993 bonds is estimated at slightly more than $300,000.

Interest rates are currently much lower than the rates on the outstanding bonds.

Refunding Bond Issue

The two refunded bond issues would be combined into one refunding bond issue.

The refunding bond issue of $8,465,000 includes issuance costs estimated at approximately $35,000.

Internal Revenue Service Requirements

Under Internal Revenue Service regulations, a current refunding must occur no more than 90 days prior to the payment of the refunded bonds.

The sale of the refunding bonds would close in mid May and the refunded bonds would be called on July 1, 2003 (first call date), meeting the requirements of the 90-day time period.

Bids

The receipt and opening of bids is scheduled for 10:00 a.m. on Thursday, April 10, 2003, and the award is scheduled for 11:30 a.m. on the same day.

Bond Specifics

Average Maturity:	7.56 Years
Bonds Dated:	May 1, 2003
Interest Due:	January 1, 2004 and each July 1 and January 1 to maturity
Interest Exemption:	Exempt from federal and state taxes for individual purchasers who are Iowa residents
Principal Due:	July 1, 2005 – 2015
Optional Call:	Bonds maturing on or after July 1, 2014 are callable commencing July 1, 2013 and any date thereafter at par
Denomination:	$5,000 and integral multiples thereof

Resolutions

Copies of the resolutions, which were prepared by Ahlers Law Firm and reviewed by Springsted, Inc., are available from the Board Office.