MEMORANDUM

To: Banking Committee

From: Board Office

Subject: Preliminary Resolution for the Sale of up to $7,000,000 Academic Building Revenue Refunding Bonds, Series S.U.I. 2004

Date: March 1, 2004

Recommended Action:

Recommend that the Board adopt A Resolution (see G.D. 3) authorizing the Executive Director to fix the date or dates for the sale of up to $7,000,000 Academic Building Revenue Refunding Bonds, Series S.U.I. 2004.

Executive Summary:

The Banking Committee is requested to recommend that the Board adopt a resolution authorizing the Executive Director to fix the date or dates for the sale of up to $7,000,000 Academic Building Revenue Refunding Bonds, Series S.U.I. 2004.

The bond issuance schedule for calendar year 2004, adopted by the Board in November 2003, included no planned sales in April. The November memorandum noted that the schedule provided flexibility to undertake refundings in April if interest rates were favorable.

As discussed previously with the Banking Committee, interest rates are historically low and the yield curve is very steep. This scenario is particularly advantageous for current refundings (occurring within 90 days of the call date) since no escrow needs to be established.

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 since principal payments for the bond issues proposed to be refunded are scheduled to be paid from tobacco bond proceeds through July 1, 2007.

Correspondence was sent to the Tobacco Settlement Authority requesting necessary approvals; authorization to proceed with the refunding was received. Consistent with the request of the Tobacco Settlement Authority, the July 1, 2005 maturities of the outstanding bonds would not be refunded.

The proposed refunding would be a current refunding. The 2006 – 2015 maturities of the Academic Building Revenue Bonds, Series S.U.I. 1993 (originally issued in the amount of $8,935,000, with a call date of July 1, 2003) and Series S.U.I. 1994 (originally issued in the amount of $1,345,000, with a call date of July 1, 2004) would be called and principal payments made on July 1, 2004.

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 2006 and 2015 total approximately $550,000 and $470,000, respectively.

The last maturity for the refunding bonds will be 2015, consistent with the last maturity of the bonds to be refunded.

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

<u>Background</u>:

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 2.87% in 2003 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 for 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.

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.

Electronic Bidding

The Board, at its November 2001 meeting, adopted a resolution approving electronic bidding procedures.

Analysis:

Bonds to be Refunded	The proceeds from the sale of the proposed refunding bonds would be used to refund the 2006 – 2015 maturities of the Board's Academic Building Revenue Bonds, Series S.U.I. 1993 and Series S.U.I. 1994. The principal to be refunded for the two issues totals $6,650,000. The 1993 bonds were issued to finance construction of an addition to the Pharmacy Building at the University of Iowa. • Coupon rates on the 2006 – 2015 maturities of the 1993 bonds range from 4.3% in 2006 to 4.6% in 2015. The 1994 bonds were issued to refund the outstanding principal of the S.U.I. Series 1991 Academic Building Project Notes. • The notes were issued to finance, in part, the remodeling of MacLean Hall and the planning for an addition to the Pharmacy Building after appropriations made by the 1989 General Assembly were deappropriated during the 1991 session. (The notes provided short-term financing pending a long-term funding source.) • Coupon rates on the 2006 – 2015 maturities of the 1994 bonds range from 4.7% in 2006 to 5.0% in 2015. Current interest rates for bonds maturing in 2006 – 2015 are significantly lower than the rates being paid on the outstanding bonds.
Refunding Bond Issue	The size of the refunding bond issue would not exceed $7,000,000, including issuance costs estimated at approximately $48,000.
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, 2004, meeting the requirements of the 90-day time period. A copy of the resolution authorizing the Executive Director to fix the date or dates for the sale of the bonds, which was prepared by Ahlers Law Firm and reviewed by Springsted, Inc. is available from the Board Office. The resolution includes a provision permitting the Board to receive bids by means of both sealed and electronic communication; the receipt by electronic communication is consistent with the resolution adopted by the Board in November 2001 approving the electronic bidding procedures.