

CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE

Minutes

June 18, 2019

Call to Order and Roll Call

The Capital Projects and Bond Oversight Committee meeting was held on Tuesday, June 18, 2019, at 1:00 PM, in Room 169 of the Capitol Annex. Representative Walker Thomas, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Rick Girdler, Co-Chair; Representative Walker Thomas, Co-Chair; Senators Christian McDaniel and Robby Mills; Representatives Steven Rudy, Steve Sheldon, and Maria Sorolis.

Guests: Doug Hendrix, General Counsel, Kentucky Communications Network Authority; Steve Murphy, Chief Financial Officer, Kentucky Communications Network Authority; Mike Hayden, Chief Operating Officer, Kentucky Communications Network Authority; Tom Howard, Partner, Commonwealth Economics; Janice Tomes, Deputy State Budget Director; Donna McNeil, Executive Director, Kentucky Infrastructure Authority; Ryan Barrow, Executive Director, Office of Financial Management; and David Carlsen, Chief Financial Officer, Kentucky Higher Education Assistance Authority/Kentucky Higher Education Student Loan Corporation.

LRC Staff: Katherine Halloran, Committee Staff Administrator; Julia Wang, Legislative Analyst; and Jenny Wells Lathrem, Committee Assistant.

Representative Thomas opened the meeting by inviting members, staff, and guests to join him in reciting the Pledge of Allegiance.

Approval of Minutes (May 14, 2019)

Representative Rudy moved to approve the minutes of the March 19, 2019 meeting. Representative Sheldon seconded the motion and the committee approved the minutes by voice vote.

Correspondence and Information Items

Ms. Halloran referenced three information items. Pursuant to KRS 45A.180(2), the University of Kentucky (UK) reported its intent to use the construction management-at-risk project delivery method for two projects within the Improve Good Samaritan Hospital Facilities pool.

Pursuant to KRS 45.760(5), the University of Kentucky and the University of Louisville reported medical and research equipment purchases.

Pursuant to KRS 45.812(1), the Danville Independent and Warren County school districts reported bond issues with locally-funded debt service to finance new projects.

Kentucky Communications Network Authority

The Kentucky Communications Network Authority (KCNA) submitted the Kentucky Bond Development Corporation (City of Williamsburg, Kentucky) Revenue Bonds, Series 2019 in an amount not to exceed \$110 million as authorized by KRS 154.15-020(4) to pay KentuckyWired project costs, capitalized interest through fiscal year 2021, and costs of issuance. The bonds will be secured by a lease with the Finance and Administration Cabinet. The cabinet will make the lease payments with future legislative appropriations.

KentuckyWired project construction is continuing with fiber installed each month, particularly in Rings 1A, 1B, and 2. Make Ready Construction, making the poles ready for new fiber, is continuing in Rings 3, 4, and 5. The contractor anticipates finishing construction prior to the revised system completion date in 2020, with some rings completed ahead of schedule.

The co-borrower's, KCNA and the KentuckyWired Infrastructure Company (KWIC), financial advisors are Commonwealth Economics and Public Resources Advisory Group. The issuer, the Kentucky Bond Development Corporation (KBDC), is an affiliate of the Kentucky League of Cities (KLC) and the sponsor city is the City of Williamsburg. The method of sale is direct purchase by Morgan Stanley. The first call date will be September 1, 2029, with a 2049 final maturity. There are no premiums associated with the call provisions. The amount borrowed is estimated to be \$104.360 million, which with the associated premium brings the total sources to \$118.960 million. The project fund deposit, approximate capitalized interest, and approximate costs of issuance will be \$110 million, \$8.26 million, and \$700,000 respectively. Annual debt service will be around \$6.9 million after expenditure of the capitalized interest proceeds.

The \$110 million will fund the \$93 million payable to the design-builder, \$88 million for settled claims and a \$5 million settlement for Supervening Event 3; unfunded project costs; and an early completion payment to the design-builder if system completion occurs prior to May 2020. Of the \$93 million, KCNA has paid about \$46 million so far, about \$44 million from the state which will be reimbursed from the bond proceeds and about \$2 million from project funds.

In response to Senator McDaniel, Mr. Murphy said that the early completion payment is the design-builder's negotiated share in the savings associated with early

migration to the KentuckyWired sites. With early migration, payments to third-party providers are discontinued sooner. KCNA's calculation of the early completion payment is around \$3 million, based upon current payments to third-party providers, and the design-builder's calculation is around \$8 million.

KCNA and KWIC's boards as well as the City of Williamsburg approved the debt issuance. Mr. Hendrix stated that KWIC is a Chapter 273 Kentucky non-profit corporation run by a board comprised of the Secretary of the Executive Cabinet, the State Budget Director, and KCNA's Executive Director. KCNA is attached to the Office of the Governor and is part of the General Government Cabinet. KWIC would not assume any liability for this debt issuance in the event of a default.

Mr. Howard said the borrowers used KBDC rather than the Kentucky Economic Development Finance Authority (KEDFA) to differentiate this debt, secured by future general fund appropriations, from the KEDFA 2015 Series A, Series B, and Series C debt, secured by availability payments. Mr. Murphy stated that availability payments are due irrespective of any savings from not having to pay third-party providers. Mr. Howard stated that the proposed issue should yield a lower rate than the interest rate, similar to the most recent state office building transaction rated A1 by Moody's.

Mr. Hayden said that contractors tested Ring 1A fiber in April, found damage to the cable primarily due to squirrel bites, and have since replaced multiple spans of fiber. This week, contractors completed final testing of Ring 1A and are testing the nodes on the network as well as the commonwealth's Alternate Data Center in Frankfort. On the I-75 spine from Lexington to Somerset, contractors repaired damage to the fiber between Richmond and Somerset and finished final testing this morning. Mr. Hayden said that the design-builder produced a schedule with projected completion dates as well as a forecast schedule with earlier completion dates.

In response to Representative Sheldon, Mr. Howard said that the upfront issuance expenses would be amortized over the term of the bond issue and that the indexed interest cost would be fixed when the parties signed the purchase agreement. Mr. Murphy commented that the estimated 3.97 percent all-in true interest cost compared favorably to the KEDFA Series A and B debt, with nearly five percent interest costs; the Series C debt, with a 10 percent interest cost; and the high equity cost on the original transaction. Mr. Murphy agreed that the KEDFA debt's lower BBB rating contributed to the higher interest costs.

In response to Representative Rudy, Mr. Howard said that interest rates were higher when House Bill 509 was filed earlier this year, decreasing the available proceeds by about \$10 million. Also, a public sale may have required an \$8 million debt service reserve fund. Therefore, the borrowers decided to pursue private placement alternatives. The debt

issuance is allowed under KRS 103.200 et seq., the industrial revenue bond statutes, and KLC suggested the City of Williamsburg as the sponsor city.

In response to Senator Mills, Mr. Murphy said the Series A, B, and C debt issuance totaled around \$306 million. There was also the approximate \$40 million in availability payments during construction; \$30 million direct contribution from the commonwealth; \$23.5 million milestone payment, funded from a federal grant; and sponsors' equity contribution. The availability payments are currently around \$30 million per year and include debt service, maintenance, operations, and sponsors' return.

Senator McDaniel commented that the difference between the payments to finance the project versus future payments to a private provider are unknown.

In response to Senator Girdler, Mr. Murphy said the \$23.5 million milestone payment through the Center for Rural Development will be remitted upon completion of Ring 1B. Mr. Hayden said there could be around \$16 million in additional federal funding.

Senator Girdler moved to approve the KBDC bond issuance, seconded by Representative Sheldon. Senator McDaniel stated that that he knew KCNA staff were working diligently and that his nay vote was not a reflection on KCNA. Representative Sorolis expressed concerns about the \$5 million difference between KCNA's and the design-builder's calculations of the early completion payment, that contractual ambiguities needed to be addressed before further funding. The motion failed to pass with two aye votes, 4 nay votes, and one pass vote.

Project Report from the Finance and Administration Cabinet

Janice Tomes reported a \$3,197,186 project under House Bill 200 (2018-2010 biennial budget bill), Part II (4), financed through three separate bond-funded maintenance pools authorized over the last three biennia. The Cabinet for Health and Family Services, Department for Behavioral Health, Development and Intellectual Disabilities, Western State Hospital - HVAC Repairs and Patient Safety Enhancements project will address compliance issues with ceilings, communal bathrooms, and hydronic piping in 10 wards.

Representative Thomas mentioned that the project was in his district.

Report from the Office of Financial Management Kentucky Infrastructure Authority

Representative Rudy moved to roll the Clean Water State Revolving Fund (Fund A) loans and the Drinking Water State Revolving Fund (Fund F) loan into one roll call vote, seconded by Senator Mills, and approved by voice vote.

Donna McNeil presented four KIA loans. The City of Louisa, Lawrence County, requested a \$3,339,588 Fund A loan, of which KIA will apply \$1 million in principal

forgiveness, incorporating a prior \$232,666 planning and design loan. The Inflow & Infiltration Rehabilitation project will separate the combined sewer and storm water collection system in the downtown area by installing 5,230 linear feet of 8-inch polyvinyl chloride sewer pipe and 3,930 linear feet of 12-inch to 42-inch high density polyethylene storm water pipe. The sewer and water rates, effective May 1, 2018, included annual adjustments above the Consumer Price Index. For 4,000 gallons, the monthly respective inside and outside city rates are \$43.28 and \$46.88 for sewer and \$39.05 and \$50.42 for water. The term is 20 years at a 0.50 percent interest rate.

The Paducah McCracken County Joint Sewer Agency (JSA), McCracken County, is requesting two Fund A loans for projects addressing a consent judgment. JSA's first loan request, \$5.193 million, is for the Perkins/Crooked Creek Wet Weather Tank project. The project will control and transport wet weather flows near the Perkins Creek and Crooked Creek sewer interceptors' intersection to eliminate a sanitary sewer overflow. Construction includes a three million gallon above ground storage facility, an influent diversion structure, a five million gallon per day pump station, and 1,000 linear feet of 18-inch and 400 linear feet of 24-inch sewer pipe.

JSA's second loan request, \$2,476,652, is for the Massac Creek Phase III project to eliminate sanitary sewer overflows and decommission four lift stations, by moving dry and wet weather flows from the Perkins Creek interceptor to the Massac Creek interceptor. Construction includes improvements to the Ross Lift Station, an additional pump and new emergency generator, as well as 8,300 linear feet of gravity sewer and 2,700 linear feet of force main.

Effective July 1, 2017, for 4,000 gallons, the JSA's monthly sewer rate is \$23.32. The term for both loans is 20 years at a two percent interest rate.

The City of South Shore, Greenup County, is requesting a \$3,051,133 Fund F loan, of which KIA will apply \$1.3 million in principal forgiveness. The New South Shore Water Treatment Plant project will improve drinking water quality in the city's service area, including northwestern Greenup and northeastern Lewis Counties, with a one million gallon per day ground water treatment plant replacing one built in the 1930's. The new 3,000 square feet facility will accommodate a fourth filter, if needed. Effective July 1, 2019, for 4,000 gallons, the respective monthly inside and outside city water rates are \$31.24 and \$33.60. The term is 20 years at a 0.50 percent interest rate.

In response to Senator McDaniel, Ms. McNeil said that for utilities qualifying for the disadvantaged community rate, KIA may offer principal forgiveness of up to fifty percent of the loan amount, \$1.3 million maximum, and a thirty year loan term. The cities of Louisa and South Shore opted for twenty year loan terms. When KIA considers principal forgiveness, which it applies after close-out of the project, it reviews the service population's affordability index relative to other projects it and the Division of Water will

include in the Intended Use Plan. Ms. McNeil said that the disadvantaged community rate qualification is based upon state criteria, when the service population's median household income is at or below 80 percent of the commonwealth's median household income; \$37,200 in the 2020 Intended Use Plan, an increase from the amount in the 2019 Intended Use Plan.

Representative Rudy moved to approve the KIA loans, seconded by Representative Sheldon, and approved by unanimous roll call vote.

New Debt Issues

Ryan Barrow submitted two new debt issues. The first was the Kentucky Higher Education Student Loan Corporation (KHESLC) Student Loan Backed Notes in an amount not to exceed \$325 million. KHESLC will use the proceeds to finance or refinance federally guaranteed Federal Family Education Loan Program (FFELP) loan acquisitions. Between \$120 million and \$125 million will be used for primarily rehabilitated FFELP loans that KHESLC either expects to purchase as part of its routine FFELP loan acquisitions through fiscal year 2020 or already purchased through interim financing sources, lines of credit or its own operating funds. KHESLC will use the additional authorized amount to acquire FFELP loan portfolios from banks or other states, if available. The \$120 million and \$125 million will be a London Interbank Offered Rate (LIBOR) based transaction with a June 1, 2049 final maturity. KHESLC typically issues debt for FFELP loan acquisitions every 12 to 18 months and its last issuance for FFELP loan acquisitions was in December 2017.

In response to Senator McDaniel, Mr. Carlsen said FFELP was eliminated in 2010 prospectively for new originations. KHESLC permanently finances its FFELP loan purchases through either LIBOR floating rate note or direct purchase note transactions. FFELP loan balances are federally guaranteed, at either 97 percent or 98 percent depending upon the first disbursement date, irrespective of student loan forgiveness.

In response to Representative Sheldon, Mr. Carlsen said that KHESLC requested the additional authorization for potential FFELP loan portfolio acquisitions from banks or other states because if such loan portfolios become available, then KHESLC may only have about three to four weeks to submit bids.

Senator McDaniel moved to approve the new debt issue, seconded by Representative Sheldon, and approved by unanimous roll call vote.

The second debt issue was the Murray State University General Receipts Refunding Bonds, 2019 Series A. The transaction will current refund outstanding 2009 Series A bonds and pay associated costs of issuance. Estimated issuance amount is \$4.3 million, with net present value savings of just under \$300,000, about \$30,000 per year.

Representative Thomas commented that no amount of savings is too small for executing the refunding transaction.

Representative Rudy moved to approve the new debt issue, seconded by Senator McDaniel, and approved by unanimous roll call vote.

School District Bond Issues with School Facilities Construction Commission (SFCC) Debt Service Participation

Ryan Barrow submitted a school district bond issue, estimated amount of \$635,000, with 100 percent SFCC debt service participation for a roof replacement project in the Lincoln County School District.

Senator McDaniel moved to approve the school district bond issue, seconded by Representative Sheldon, and approved by unanimous roll call vote.

Representative Thomas said that the next committee meeting would be held Tuesday, July 23 at 1:00 p.m. in Annex Room 169, a week later than usual.

With there being no further business the meeting adjourned at 1:54 p.m.