

COUNTY OF MILWAUKEE
INTEROFFICE COMMUNICATION

DATE : September 2, 2014

TO : Supervisor Dimitrijevic, Chairwoman, County Board of Supervisors

FROM : Josh Fudge, Director, Office of Performance, Strategy, and Budget
Pamela Bryant, Capital Finance Manager, Office of the Comptroller

SUBJECT : Reallocation of Unspent Bond Proceeds and Adoption of New Capital Budget Financing Policies

REQUEST

To comply with the Internal Revenue Service (IRS) expenditure rules for bonds, the Office of the Comptroller and the Department of Administrative Services - Office of Performance Strategy and Budget (DAS-PSB) are seeking approval to reallocate approximately \$1.6 million of 2009-2013 unspent bonds from the debt service reserve and from capital projects that continue to be delayed or have surpluses to capital projects that have incurred deficits or are urgent. The projects that are financed with bonds issued in 2009-2010 are not compliant with IRS expenditure rules because the County has not been able to demonstrate a consistent pattern of spending that reflects a commitment to implementation. Therefore, this request relating to the transfer of unspent bond proceeds on capital projects is being done to comply with IRS rules.

The active capital projects are financed with bonds issued in 2009-2013 and soon to be issued in 2014. The expenditure deadlines for the bonds from 2009-2013 are listed below. The County did not issue any corporate purpose (general, non-airport bonds) in 2011 and 2012. With the exception of the 2013 bonds, all of the bonds issued in 2009 and 2010 should have been expended.

Table 1: Unspent Bonds by Bond Issue Year/Series

Bond Issue	Amount Unspent *	Closing Date	Expenditure Deadline
2009C	\$70,677	8/1/2009	8/1/2012
2009D	\$54,838	8/1/2009	8/1/2012
2009E	\$265,292	11/15/2009	11/15/2012
2009F	\$296	11/15/2009	11/15/2012
2010A	\$589,191	5/1/2010	5/1/2013
2010B	\$19,104	5/1/2010	5/1/2013
2010C	\$425,508	12/21/2010	12/21/2013
2013A	\$211,514	8/14/2013	8/14/2016
Total	\$1,636,420		

*The unspent balance amounts are as of 8/26/14. If activity changes the dollar amounts prior to a transfer being processed after final board adoption, an amount as close to the current unspent amount as possible will be transferred.

The Office of the Comptroller is also requesting reallocation of budgeted sales tax revenue of approximately \$550,000 from existing projects to the newly created Project WO217 Phone and Voicemail Replacement. The existing projects will have their financing replaced with unspent bonds in order to assist the County with complying with IRS rules.

Furthermore, the Office of the Comptroller and DAS-PSB are also requesting the adoption of policies to help address the overall issue of expending general obligation bonds in accordance with IRS rules. These changes include the following:

Limit the Time for Spending of Bond Financed Projects

The IRS regulations dictate the expenditure of bond proceeds within three years of the date of issuance of the bonds. After three years the County must “yield restrict” the remaining unspent bonds proceeds and must demonstrate a consistent pattern of spending to reflect a commitment to implementing the projects, otherwise the County could be subject to IRS action. In order to avoid those issues, it is recommended that Capital projects that have unspent bonds be lapsed after a period of four years and have proceeds applied towards debt service for the bonds or reallocated to another project.

Limit Capital Projects to Those Estimated to Cost More Than \$100,000

Increasing the financial threshold for projects to be included within the capital budget to \$100,000 would reduce the total number of projects that would need to be managed in accordance with the IRS rules. This would allow for better monitoring of the remaining projects and a greater likelihood that projects would be able to comply with the IRS spending guidelines. The Office of the Comptroller and the Department of Administrative Services recommend that future Capital Improvement Budgets include a policy of limiting projects in the capital improvements budget to those estimated to cost more than \$100,000.

BACKGROUND

At year-end 2012, the estimated total unspent bond balance was \$44.2 million for 219 capital projects.

In April 2013, the Office of the Comptroller included language in the 2012 to 2013 Carryover Report informing policymakers that the County was not in compliance with IRS expenditure rules for bonds.

In May 2013, a review by the Office of the Comptroller determined that \$13.3 million in unspent bond proceeds should be reallocated to other projects that presumably could move forward in an expeditious fashion.

In June 2013, the County Board and County Executive approved Resolution 13-537 that reallocated approximately \$5.8 million of unspent bonds to projects that were adopted as part of the 2013 Capital Improvements Budget.

In July 2013, the County Board and County Executive approved Resolution 13-633 that reallocated \$7.5 million of unspent bonds to projects that included as part of the County’s Five-Year Capital Improvement Plan.

At year-end 2013, the estimated total unspent bond balance was \$38.1 million for 238 capital projects.

In March 2014, the Office of the Comptroller received approval of initial authorizing resolution and final bond resolutions (14-171) in an amount not-to-exceed \$42 million.

IRS Expenditure Rules for Tax Exempt Bonds

The IRS regulations dictate the expenditure of bond proceeds within three years. If the bond proceeds have not been expended within three years, according to Quarles and Brady (the County's Bond Counsel), the IRS expectation is that the County will proceed or demonstrate a consistent pattern of spending to reflect a commitment to implementing the projects.

In addition, the County cannot invest the unspent bond proceeds in investments having a yield greater than the yield on the bonds. The County is complying with the requirement regarding investment yield since the investment yield is currently lower than the yield on the bonds. If investment rates increase, the County could have a problem identifying investments with yields lower than the yield on the bonds. The penalty for not complying with the investment rate restriction could be monetary or could be a loss of the subsidy payments on the Build America Bonds.

Furthermore, the County is limited in terms of the type of investments of bond proceeds that are beyond the IRS expenditure timeline. The bond proceeds cannot be invested in (i) federally insured deposits or accounts (as defined in Section 149(b)(4)(B) of the Code), or (ii) investments constituting obligations of or guaranteed, directly or indirectly, by the United States of America (except obligations of the United States Treasury or investments in obligations issued pursuant to Section 21B(d)(3) of the Federal Home Loan Bank Act, as amended (e.g., Refcorp Strips).

ANALYSIS

Allocation of Unspent Bond Proceeds

Since the IRS expectation is that the County will proceed or demonstrate a consistent pattern of spending to demonstrate a commitment to implementation, approximately \$1.6 million is recommended to be reallocated.

As of August 2014, there was approximately \$28 million in unspent bond proceeds. The Office of the Comptroller and the DAS-PSB met with departments to discuss the status of the projects. Approximately \$1.3 million in unspent bonds from projects is included below in Table 2. The total amount of unspent bonds is approximately \$1.6 million, including approximately \$300,000 transferred from the debt service reserve. The remaining \$26.7 million is financing active projects.

Table 2: Projects With Reallocated Unspent Bonds

<u>Project Description</u>	<u>Unspent Bond</u>	
	<u>Amount *</u>	<u>Bond Year/Series</u>
WP07025 Lindberg Park Wading Pool Roof	\$53,319	2013A
WP25702 KK Sports Complex #1 Fencing	\$2,219	2013A
WC07001 Domestic Violence Area Reconstruction	\$30,630	2013A
WO06011 KK River Parkway 57th St. to 60th St.	\$23,769	2013A
WO07301 Underwood Creek Parkway- OLT Program	\$76,617	2013A
WO22103 Data Center Equipment and Construction	\$590	2013A
WP25101 Parks Maintenance Shop Roof	\$72,170	2009C/2009D
WS03201 Variable Air Volume Boxes	\$1,469	2009E
WG01201 1000 MG Waterspheroid	\$59,759	2009E
WC02501 Courthouse Restroom Renovation	\$179,504	2009E
WJ05101 HOC Security Camera System	\$11,220	2009E
WZ10301 Zoo Train Garage Overhead Crane	\$6,389	2010A
WZ11401 Zoo Life Support Emergency Generators	\$1,445	2010A
WZ11501 Great Apes Mechanical Roof Replacement	\$2,060	2010A
WS03801 Coggs Canopy Renovation	\$91,584	2010A
WC03801 Courthouse Roof Drain	\$86,055	2010A
WC07101 DA Security Card System	\$5,200	2010A
WC086 City Campus Cooling Towers Replacement	\$75,071	2010A
WO22102 Clean Agent Fire Suppression	\$131,893	2010A
WP25201 Root River Parkway Lighting System	\$19,104	2010?
WV01401 Dratzka Park Ground Water and Soil	\$8,703	2010C
WP06901 Countywide Play Area Redevelopment	\$18,936	2010C
WP17209 Kosci Aquatic Center Building Roof	\$29,961	2010C
WP20001 Jackson Park Boathouse Roof	\$48,129	2010C
WP22901 Dineen Parking Lot and Walkway	\$20,236	2010C
WP28101 Scout Lake Pavilion Roof Replacement	\$7,727	2010C
WP395 Parks Boiler/Furance/AC Replacements	\$22,829	2010C
WZ01462 Zoo ARC HVAC Replacement	\$3,000	2010C
WZ01463 Seal Pool Filer Room Rehabilitation	\$2,419	2010C
WV02501 Rawson Avenue Pump Station	\$216,781	2010C/2013A
Debt Service Reserve	\$327,632	Various
Total	\$1,636,420	

*The unspent balance amounts are as of 8/26/14. If activity changes the dollar amounts prior to a transfer being processed after final board adoption, an amount as close to the current unspent amount as possible will be transferred.

Allocation of Unspent Bond Proceeds to Projects that Require Additional Funding

The Office of the Comptroller has reviewed existing capital projects. Based on this analysis, there are eight (8) ongoing projects that require additional funding of \$680,000.

In addition, during discussions with the Department of Administrative Services – Facilities Management Division, it was noted that the Safety Building needed \$100,000 for the replacement of the emergency generator. The Safety Building Emergency Generator was activated during the July 2013 Courthouse fire power loss. The emergency backup generator is designed to bridge a temporary power loss, not an indefinite prolonged outage. Due to the extended power loss the generator ran continuously until the motor blew a piston. Currently, the portion of the Safety Building that would normally receive service from the damaged generator is being backed up by a temporary generator located on 9th Street. The current generator will need to be replaced since it is undersized and repair parts are not available.

A list of these projects that require additional funding (\$780,000) is included in Table 3.

Table 3: New/Ongoing Projects that Require Additional Financing

<u>Project Description</u>	<u>Unspent Bond Amount</u>
WP25101 Parks Maintenance Shop Roof	\$210,000
WG01701 Vel Phillips Fire Protection System	\$150,000
WG01801 Research Park Fire Protection System	\$28,000
WG01901 CATC Fire Protection System	\$64,000
WV02901 Grant Park Lift Station	\$100,000
WO43301 Glass Barrier at CJF	\$62,000
WC11401 Safety Building Emergency Generator	\$100,000
WZ11501 Great Apes Mechanical Room Roof Replacement	\$66,000
Total	\$780,000

Exchange and Reallocation of Sales Tax Revenue

There are five ongoing projects that are currently financed by sales tax that could be financed with unspent bonds. These projects have demonstrated a consistent pattern of spending that makes them good candidates to be financed with the unspent bond proceeds. The total amount of sales tax that will be exchanged for unspent bond proceeds is approximately \$550,000.

In addition, the exchanged sales tax revenue is recommended to be used to finance a new Phone and Voicemail Replacement project. During discussions with the Department of Administrative Services – Information Management Services Division, it was noted that the County’s current PBX phone system was in urgent need of replacement. Many of the County’s facilities have phone systems that are no longer manufactured nor supported. The approximately \$550,000 being requested to finance this project will be used to hire a consultant to develop a plan for replacing the County’s phone system, replace the current systems at the Zoo and the House of Correction and to make any critical repairs to the County’s current phone system that are needed prior to replacement. Ongoing projects proposed for the sales tax exchange with unspent bonds and the addition of the Phone and Voicemail Project are listed in Table 4.

Table 4: Exchange and Reallocation of Sales Tax Revenue

<u>Project Description</u>	<u>Sales Tax Amount</u>	<u>Unspent Bond Amount</u>
WG01701 Vel Phillips Fire Protection System	(\$197,340)	\$197,340
WG01801 Research Park Fire Protection System	(\$87,340)	\$87,340
WG01901 CATC Fire Protection System	(\$9,382)	\$9,382
WP46201 Dineen Park Tennis Courts Replacements	(\$150,000)	\$150,000
WP46301 Tiefenthaler Park Area Play Area Replacement	(\$108,000)	\$108,000
WO219 Phone and Voicemail Replacement	\$552,062	
Total	\$0	\$552,062

Reduction of 2014 Corporate Purpose Issuance

The Research Park Fire Protection System project and the CATC Fire Protection System project were financed with bonds to be issued in 2014. Since unspent bond proceeds are available, they will be used to finance these two projects. The 2014 bond issue will be reduced by \$304,358.

RECOMMENDATION

Reallocations/Exchanges

The Office of the Comptroller and the DAS-PSB recommend adoption of the attached resolution. The resolution authorizes the reallocation of approximately \$1.6 million of unspent bonds from selected projects and the debt service reserve. The resolution also changes financing for several capital project from sales tax revenue to unspent bond proceeds. If activity changes the dollar amounts prior to a transfer being processed after final board adoption, an amount as close to the current unspent amount as possible will be transferred.

The resolution also authorizes the creation of two new capital projects: Project WC114 Safety Building Emergency Generator (\$100,000) and Project WO217 Phone and Voice Mail Replacement (\$552,062) In addition, the resolution directs the DAS to process an administrative transfer to effectuate the reallocations/exchanges and to create the new capital projects.

Capital Budget Financing Policies

The Office of the Comptroller and the DAS-PSB are also recommending the adoption of policies to help address the expenditure of bonds overall. These changes include the following:

- Limit the time for spending of bond financed projects to a period of four years. After four years, the projects will be abandoned and the proceeds applied towards debt service for the bonds or reallocated to another project.
- Limit projects that can be included in the capital budget to projects that are estimated to cost greater than \$100,000.



Josh Fudge
Director, Department of Administrative Services- PSB



Pamela Bryant
Capital Finance Manager, Office of the Comptroller

pc: Chris Abele, County Executive
Supervisor Willie Johnson, Co-Chair, Committee on Finance, Audit and Personnel
Supervisor David Cullen, Co-Chair, Committee on Finance, Audit and Personnel
Rex Queen, Deputy Treasurer, Office of the Treasurer
Don Tyler, Director, Department of Administrative Services
Raisa Koltun, Chief of Staff, County Executive's Office
Kelly Bablitch, Chief of Staff, County Board
Vince Masterson, Department of Administrative Services
Stephen Cady, Office of the Comptroller
Justin Rodriguez, Office of the Comptroller
Greg High, Department of Administrative Services- AE&ES
James Keegan, Parks
Gary Waszak, Department of Administrative Services- Facilities
Brian Lanser, Quarles and Brady
Bridgette Keating, Quarles and Brady