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Authority to Sell or Lease State Properties -- Use of Proceeds (Administration and Building Commission)

[LFB 2013-15 Budget Summary: Page 40, #6 (part) and Page 83, #8 (part)]

CURRENT LAW

With specific exemptions, the Department of Administration (DOA) may offer for sale certain state-owned property when it determines the sale is in the best interest of the state. The proceeds from the any DOA sales of state properties must first be used to retire any outstanding debt related to the facility sold. Sale proceeds must be used to repay the federal government if required by law and, if the property was acquired by gift, the sale proceeds are subject to any restrictions governing the use of the proceeds. Any remaining proceeds must be used to retire other outstanding public debt. To the extent practical, the DOA Secretary must consider certain factors in determining which public debt to redeem, including according preference to the redemption of general obligation debt within the same statutory bond purpose that was used to acquire, build, or improve the property being sold.

The Building Commission has authority to sell certain property, including surplus property. The net proceeds from the sale of property must be used to retire any outstanding debt related to that property. Remaining sale proceeds are deposited to the budget stabilization fund.

GOVERNOR

Specify that the DOA Secretary or the Building Commission, to the extent possible, must consider the following in determining which public debt to redeem: (a) the extent the debt service on the property being sold or leased was paid from a segregated fund, other outstanding debt related to that fund should be redeemed; (b) the extent to which general obligation debt was issued to acquire, build, or improve the property is subject to current optional redemption, would require the establishment of an escrow, or could be assigned for accounting purposes to a statutory bond purpose; (c) the fiscal benefit of redeeming outstanding debt with higher interest costs; and (d) the costs of maintaining federal tax law compliance in the selection of general obligation debt to be redeemed. In addition, specify that if the net proceeds exceed the amount required to be deposited, paid, or used for other purposes, with certain limited exceptions, DOA or the Building Commission would be required to use the net proceeds or the remaining net proceeds to pay principal and interest costs on other similar revenue obligations.

Specify that if there are any outstanding revenue obligations issued to finance the acquisition, construction, or improvement of any property that is sold or leased by DOA or the Building Commission, the Department or Commission would be required to deposit a sufficient amount of the net proceeds from the sale or lease of the property in the respective redemption funds provided for those obligations to repay the principal and pay the interest on the obligations, and any premium due upon refunding any of the obligations. Require DOA or the Building Commission to provide a sufficient amount of the net proceeds from the sale or lease of the property for the costs of maintaining federal tax law compliance applicable to the revenue obligations. Specify that for the purpose of paying principal and interest costs on other outstanding revenue obligations, the Department and the Building Commission could cause such obligations to be called for redemption on or following their optional redemption date, establish one or more escrow accounts to redeem obligations at their optional redemption date, or purchase bonds on the open market.

Modify DOA's current authority relating to the use of proceeds from the sale of state property to include proceeds from the lease of state property. In addition to the current law requirement of retiring any outstanding principal, interest, or premium due on debt related to the property, require that DOA provide from the net proceeds from the sale or lease of state-owned real property by the Department, a sufficient amount for the costs of maintaining federal tax law compliance applicable to any such debt. Specify that these same provisions would apply to property sold or leased by the Building Commission.

DISCUSSION POINTS

Use of Proceeds -- Sale of State Properties

1. Under the Governor's recommendation, the proceeds from any sale or lease of state property would have to be used to retire general obligation or revenue obligation debt associated with that facility and any federal or other obligations or restrictions related to the facility or the debt on that facility. After these obligations are met, any remaining proceeds would have to be used to retire other outstanding debt obligations.

2. The bill would provide the DOA Secretary or the Building Commission with discretion to determine which outstanding debt to redeem using those remaining proceeds. Specifically, in determining which outstanding bonds to redeem, the DOA Secretary would only have to give consideration to whether the debt service on the property being sold or leased was paid from a segregated fund and consider redeeming other outstanding debt related to that fund. However, The DOA Secretary would not be required to use the remaining net proceeds from the sale of a state property to retire other debt on other properties held by the agency whose property was sold. While this discretionary authority on which debt could be redeemed from state property

sales proceeds may be similar to current law, the DOA Secretary and the Building Commission would have significantly broader authority to sell or lease state property under the bill.

3. Staff from DOA indicate that one of the primary reasons for requesting the authority to sell or lease state-owned facilities is so that the proceeds from the sale of those assets can be used to retire outstanding state debt. Specifically, it is the administration's intention to use any property sale proceeds to retire state transportation-related debt in order to offset a portion of the transportation debt authorized under the budget bill ($994.2 million in total). This could include past GPR-supported transportation related debt to offset some of the $200 million in GPR supported transportation debt recommended to fund a portion of the Zoo Interchange highway project. The Department of Transportation Secretary, after acknowledging concerns related to the level of transportation bonding under the bill, also indicated in testimony before the Joint Finance Committee that proceeds from the sale of state assets would be used to retire GPR supported transportation-related bonding.

4. No direct link exists in the bill that would specifically direct the remaining proceeds from asset sales toward the payment of principal on outstanding bonds issued for transportation purposes. Rather, the DOA Secretary would be provided broad authority to apply any remaining proceeds from the sale of state properties to the repayment of debt. While the DOA Secretary and DOT Secretary indicated the GPR supported transportation bonding would be targeted, the state has issued both GPR supported and SEG (transportation fund) supported bonding for transportation-related purposes. Under the Governor's recommendations, the DOA Secretary or the Commission could target the proceeds from the sale of state properties to redeem either type of transportation-related debt, or any other state debt.

5. Staff from DOA indicate that the proceeds from sale or leases of state property would probably not be used to retire the specific $200 million in GPR supported bonds that could be issued for the Zoo Interchange road project under the bill. Rather, the authority provided to the DOA Secretary under the bill is purposely broad so as to allow him to use any remaining proceeds from the sale of state properties to redeem the specific outstanding bonds that would be in the best interest for the state to retire. The rates, call provisions, and other terms of state's debt obligations make redeeming certain bonds more financially favorable than other bonds. While the focus would likely be transportation-related debt, the authority provided the Secretary would allow flexibility to ensure that the bonds chosen to be redeemed would make the most sense financially for the state to retire.

6. One concern about the broad authority on the use of property sale proceeds provided under the bill is that the DOA Secretary or the Building Commission could sell a state property that was funded from one revenue source and use any remaining proceeds from that property sale to retire debt backed by a different funding source. For example, under the bill, the DOA Secretary or the Building Commission could sell a Department of Administration property, UW System property, or the property of any other agency, and use the proceeds from the sale of those properties to retire debt issued for transportation purposes. As an example, it would be possible for the DOA Secretary to sell a dormitory facility at UW River Falls, which is funded from the housing fees paid by students, some of which are used to retire debt on that dormitory facility. The DOA Secretary

could then apply the remaining proceeds from the sale of the dormitory facility to retire outstanding state debt issued for state highway improvements or highway rehabilitation projects. It may not be the intention of the DOA Secretary or Building Commission to carry out such a transaction, but it would be allowed under the bill.

7. A general budgeting principle is that dedicated fees or taxes, whether deposited as program revenues or segregated revenues, are established to pay for the service for which the fee or tax is being imposed. This principle is the general reasoning behind Senate Joint Resolution 4 (SJR 4), a proposed constitutional amendment, which passed second consideration earlier this session. SJR 4 would essentially require that transportation-related taxes and fees be deposited in the transportation fund and used for transportation-related purposes. Allowing the DOA Secretary or Building Commission to use proceeds from the sale of state property funded from non-transportation-related program and segregated revenues to retire outstanding transportation-related debt, whether supported by the general fund or the transportation fund, would seem counter to this principle.

8. A separate concern, specific to the use of proceeds associated with the sale of state utility plants to a private utility, involves the decision as to which agency would pay for the private utility's capital costs associated with purchasing the plant. Under the bill, DOA could sell a utility plant, and use the proceeds from the sale to retire the debt on the plant, and possibly other, unrelated debt, as determined by the DOA Secretary or the Building Commission. As a result, only limited proceeds from the sale could flow to the agency whose plant was sold through the lower debt service costs associated with the retirement of the state debt associated with the utility. However, the agency would continue to need the output from that plant to heat or cool its facilities. Utility officials have indicated that the rates a private utility would charge for the output from the plant would include both the utility's operating costs and its capital costs (the cost to finance the facility purchase). Therefore, if any remaining proceeds from the sale of state utility plant would be used to redeem debt unrelated to that agency whose plant was sold, the state would reduce its indebtedness, but the individual agency whose plant is sold could experience higher operating costs. Requiring that the any excess proceeds from a sale of state property could only be used to retire debt issued under the same agency's bonding authorization purposes would more likely ensure that the agency with jurisdiction over the utility plant, and who would need to purchase the output of that plant, would also receive the full benefit of the debt service reduction associated with the sale of the plant.

9. If Committee members have concerns about using proceeds from the sale of a property to redeem outstanding debt that is unrelated to the property being sold, the Committee could require the net proceeds from the sale of a state property would have to first be used to retire debt issued under the same bonding purpose authorization that was used to finance the property being sold (Alternative 2). Under this alternative, the Committee would be requiring the DOA Secretary or the Building Commission to use any remaining proceeds from a sale to redeem outstanding debt supported by the same funding source and issued from the same agency bonding authorization that supported the initial acquisition, construction or renovation of the property.

Use of Proceeds -- Lease of State Properties

10. Under the bill, if DOA or the Building Commission were to lease a state property,

the state would receive annual lease revenues associated with property. Further, the state could potentially reduce its staffing and operation costs associated with the leased property. Other bill provisions would allow the DOA Secretary reduce agency budget and staff associated the sale or lease of that agency's property (Paper #163). Unless the property was surplus and no longer needed for agency operations, the lease revenues and the reductions in agency budgets and staff associated with the facility could be offset by continued lease costs. Because the state would continue to own the property, the state would have to service any debt on the property, and could have to maintain and finance any improvements to the facility. Any takeover of maintenance and improvements by the lessee would be reflected in reduced lease payments. In addition, if the property is still needed to provide a service, the state agency charged with providing the service would have to buy back that service from the lessee of the facility. Further, if a GPR supported facility is leased, and the proceeds from the lease are used to retire GPR supported debt, agencies may not receive GPR funding needed to cover any costs associated with buying back the service or output from the leased facility.

11. As an example, under the provisions of the bill, the DOA Secretary state could lease UW-Madison West Campus Cogeneration facility to a private utility. The annual lease revenue would have to be used to retire debt related to that plant, but would not likely be sufficient to cover the annual debt service payment on the outstanding debt of the facility. Again, it is not known whether the state or lessee would be responsible for maintaining and improving the facilities, but either way, whether through reduced lease payments or directly paying for the costs, the state would be paying some portion of these costs. While the DOA Secretary would be able to reduce UW Madison's utility plant staff, and associated funding to reflect that the institution would no longer be operating the facility, UW-Madison would now have the cost of having to purchase the output from that plant, which could offset some or all of the savings. This could create a mismatch in the institution's funding in that the institution would see a reduction in its debt service appropriation, but the institution would need additional funding in its operations appropriation to buy back the utility's output provided at the leased plant.

12. If one of the primary reasons for providing DOA and the Building Commission the authority related to the disposal of state properties is to retire outstanding debt, leasing properties may not accomplish that goal. Unlike sales of state assets, leasing assets would not provide a large, upfront, lump sum amount that could be used to offset a significant amount of debt principal. The lease revenues would come over time, while the state would continue to have ongoing costs associated with the facility. A better use of these annual lease revenues may be to pay for ongoing state costs related to the facility. Under this approach, the Committee could delete the Governor's recommendation that requires that the proceeds from the lease of state properties be used to retire outstanding debt on that property, or other outstanding debt. The use of these proceeds could be dealt with when Committee takes up Paper #163.

ALTERNATIVES

1. Approve the Governor's recommendation on the use of proceeds associated with the sale or lease of a state property by the DOA Secretary or the Building Commission.

2. Modify the Governor's recommendation and require the DOA Secretary or the Building Commission to apply any remaining proceeds from the sale of a state property, after the other specified obligations are met, to redeem debt supported by the same funding source and issued under the same bonding purpose authorization that was used to finance the property being sold.

3. Modify the Governor's recommendation and delete the requirement that net proceeds from the lease of a state property would be used to retire the outstanding debt on that facility, other obligations, or restrictions related to the property, and other outstanding state debt.

4. Delete provision.

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