NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: HB 1430 (3rd Edition)

SHORT TITLE: State Capital Facilities Financing Act

FISCAL IMPACT

Yes (X**)** **No ( )** **No Estimate Available ( )**

	FY 2002-03	FY 2003-04	FY 2004-05	FY 2005-06	FY 2006-07
EXPENDITURES - General Fund					
Debt Service*					
Repairs/Renovations		16.05	15.63	15.20	14.77
Prison Acquisitions		to be determined based on purchase price (See Assumptions and Methodology)			
Psychiatric Facility		_____	_____	11.00	10.70
Total Debt Service		16.05	15.63	26.20	25.47

PRINCIPAL DEPARTMENTS: The Department of State Treasurer, Department of Corrections, Department of Health and Human Services.

EFFECTIVE DATE: When the bill becomes law.

*The additional General Fund debt service requirements will continue through 2026-27. The total additional requirements depend on the size of the prison financing package.

BILL SUMMARY:

A. SPECIAL INDEBTEDNESS

(1) Authorizes the State to issue or incur debt for construction, improvement, and acquisition of State capital facilities and to secure the debt by a lien on or security interest in the property.

The specific authorizations for special indebtedness included in the bill are:

a. $150 million in Repairs and Renovations. The proceeds of this category of special indebtedness would be used to repair and renovate State buildings in the same manner as funds in the Reserve for Repair and Renovations are used. Except in the case of an emergency, the executive branch is required to consult with the Joint Legislative Commission on Governmental Operations before incurring debt for specific repair and renovation projects.

b. Acquisition of Prisons. These funds could be used to purchase two prisons that are currently being leased by the State from a private vendor – Pamlico and Mt. View (Avery/Mitchell).

c. Up to $100 million for Psychiatric Hospitals. These funds could be used for the construction of a new psychiatric hospital. The financing contract indebtedness could not be incurred prior to July 1, 2004. Before incurring any special indebtedness for this project, the State Treasurer may require one or more reports evidencing the savings expected to be realized from the closure of existing psychiatric hospitals that are to be replaced by the project and the feasibility of the financing of the project.

The bill contains language to prohibit the executive branch from incurring special indebtedness unless the capital projects to be financed have been specifically authorized by an act of the General Assembly and the executive branch has reported to the Joint Legislative Commission on Governmental Operations regarding the details of the debt to be incurred.

The debt would be secured by a lien on or security interest in all or any part of the capital facilities to be financed, including all or part of any land on which improvements are to be constructed. If the project is a renovation, the entire existing facility as well as the improvement could serve as security. The value of the property securing the debt may exceed the amount of the debt and the financing of several capital projects may be jointly secured by liens on some or all of the capital facilities being financed.

There would be no pledge of the State's taxing power or full faith and credit. Thus, voter approval is not necessary for the borrowing. If the State defaulted on its repayments, no deficiency judgment could be rendered against the State, but the capital facilities that serve as security could be disposed of to generate funds to satisfy the debt. The State could choose not to appropriate funds to repay the debt, but such a decision would have negative consequences for the State's credit rating.

The funds could be borrowed from a single entity in an installment purchase or lease purchase contract, could be generated by the issuance of limited obligation bonds, or could be borrowed under an installment financing contract by the sale of certificates of participation. A certificate of participation represents the holder's undivided interest in the right to receive the installment payments to be made by the State. If certificates of participation are issued, a nonprofit corporation will act as a straw person to facilitate the financing.

Before special indebtedness could be issued or incurred, the State Treasurer must certify that debt financing may be desirable for a specific project presented to it by the Department of Administration. Next, the Council of State must give preliminary approval. If preliminary approval is obtained, the Council of State must give final approval, setting out details such as the maximum amount to be financed, the maximum maturity, and the maximum interest rates. The maximum maturity may not exceed 40 years. The State Treasurer must approve the financing, finding that the amount to be borrowed is adequate and not excessive and will not require an excessive increase in any State revenues to provide for repayment, and that the special indebtedness can be incurred or issued on terms favorable to the State. Finally, the State Treasurer must report to the Joint Legislative Commission on Governmental Operations at least five (5) days before any special indebtedness is issued or incurred.

B. SPECIAL OBLIGATION BONDS

Authorizes the State to issue a maximum of $100 million in special obligation bonds for construction of a new psychiatric hospital. The bonds would be secured solely by, and payable solely from, the revenues pledged for that purpose. The bill defines the "pledged revenues" as:

a. Medicaid and Medicare reimbursements received by the State and allocated for depreciation expense of the new hospital, plus the Medicaid and Medicare reimbursements received by the State and allocated for interest on the debt used to finance the new hospital. This stream of revenue is expected to generate approximately $8.3 million over a 20-year period.

b. The funds deposited with the Department of State Treasurer as nontax revenue associated with Disproportionate Share Payments from State institutions for mental disease that are collected pursuant to Title XIX of the Social Security Act, 42 U.S.C. 1396r-4, as amended. This stream of revenue is expected to generate approximately $107 million a year for the next three to five years. Currently, this stream of revenue is appropriated for other purposes. To utilize this stream of revenue as a source of pledged revenues, a portion of it would need to be dedicated to the financing of this Project.

c. The funds appropriated to the Trust Fund for Mental Health, Developmental Disabilities, and Substance Abuse Services established under G.S. 143-15.3D last year in S.L. 2001-424.

d. Any revenues generated by the capital project – namely the savings realized from the closure of existing psychiatric hospitals that are to be replaced by the new facility.

Special obligation bonds are not general obligation bonds and thus not required to be approved by the voters. Neither the faith and credit nor the taxing power of the State would secure them and a statement to this effect would appear on the face of the bonds. Property could not be pledged to secure the bonds. The sole security and source of repayment would be from the sources of revenue defined by the act as "pledged revenues." The bill provides that no other source of funds may be used to pay the bonds. The State would not be obligated to pay the debt from other sources and a default not within the State's control would not be expected to affect its credit rating. The General Assembly could chose, however, to amend the legislation at that time to authorize the use of other State revenues to pay the debt service. Such a provision is not in the bill at this point because it could make the proposed bonds a liability of the State, which could affect the State's existing bond rating.

C. LOCAL GOVERNMENT SPECIAL OBLIGATION BONDS.

Under current law, local units can issue special obligation bonds to finance a limited list of capital projects, including primarily water and solid waste related projects. The bill expands the type of projects that can be funded under this mechanism to include items that can now only be financed through general obligation bonds. These items include airports, armories, auditoriums, coliseums, arenas, stadiums, civic centers, convention centers, facilities for exhibitions and events, beach improvements, cemeteries, facilities for fire fighting and prevention, hospitals, land for corporate purposes, law enforcement facilities, libraries, art galleries, museums, art centers, historic properties, parking facilities, parks and recreation facilities, public buildings, public vehicles, redevelopment, sewer systems, landfills, flood control facilities, voting machines, water systems, public transportation facilities, industrial parks, railroad corridors for preservation, cable television systems, electric systems, gas systems, streets and sidewalks, and telephone system upgrades. In addition, the bill authorizes cities to issue special obligation bonds to finance services, facilities, or functions provided within a municipal service district.

ASSUMPTIONS AND METHODOLOGY:

DEBT SERVICE. Repairs and Renovations Bonds. The debt service estimates were based on a June 2002 simulation of the Office of State Treasurer, modified by Fiscal Research for the smaller size. The analysis assumes a March 1, 2003, issuance date, an average interest rate of 5.7%, and a maximum maturity of 20 years.
Prison Facilities. Debt service projections are not included since the purchase price is negotiable and undetermined. The state is currently paying approximately $6 million a year to lease two prisons from a private vendor. The Office of State Treasurer estimates that if the prisons were purchased with COPS, that the savings from eliminating lease payments would exceed debt service by as much as $130 million dollars until maturity.
Psychiatric Facility. The debt service projections are based on a simulation of $100.0 million of financing. The analysis assumes a 6.0% average interest rate and a maximum maturity of 20 years. In addition, the financing would occur on March 1, 2005, in the simulation.
Local Government Special Obligation Bonds. Because these changes only expand the type of funding mechanisms available to local governments, no direct fiscal impact is expected as a result of these changes.

OPERATING EXPENDITURES. **Psychiatric Hospital.** The operating expenditure data for the new hospital, as provided by the Department of Health and Human Services, is shown below:

	FY 2003-04	**FY 2004-05**	**FY 2005-06**	**FY2006-07**	**FY 2007-08**
Operating Expenditures					
John Umstead Hospital	$51,522,470	$50,591,240	$49,646,840	$49,194,640	$0
Dorothea Dix Hospital	$50,205,227	$49,612,377	$49,200,777	$49,012,677	$0
New Psychiatric Hospital	$0	$0	$0	$0	$50,000,000
Expenditures Realigned to Community Services	$2,272,303	$3,796,383	$5,152,383	$5,792,683	$50,000,000

- Current state appropriations for operating expenditures in Umstead and Dix Hospitals provided by the Department of Health and Human Services
- Estimated operating costs for the new hospital provided by DHHS
- The reduction of operating expenditures associated with the downsizing and closure of Umstead and Dix Hospitals were developed by DHHS.
- This bill contains language that would cause any cost-savings from the downsizing and closure of Umstead and Dix **not to revert** to the General Fund. Instead, non-recurring savings would go to the Mental Health Trust Fund and recurring savings would be retained by DHHS to help fund the community-based services. The result would be no net impact to the General Fund, in terms of appropriations for operating expenditures.

FISCAL RESEARCH DIVISION: (919) 733-4910

PREPARED BY: Dave Crotts, Jim Mills, Jim Klingler

APPROVED BY: James D. Johnson

DATE: September 25, 2002

Official
Fiscal Research Division
Publication

Signed Copy Located in the NCGA Principal Clerk's Offices