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FALL 2021

A Quarterly Newsletter of the National Association of Health and Educational Facilities Finance Authorities

NAHEFFA

NAHEFFA President's Message

by Dennis Reilly, Executive Director
Wisconsin Health & Educational Facilities Authority

I would like to thank everyone who attended our Fall Conference in Milwaukee, the first in-person NAHEFFA conference in over 2-years. The conference committee put together a great agenda loaded with valuable information, great sessions, talented presenters, and some wonderful social events.

What a joy it was to see people in person again! As much as we enjoy the convenience and ease of virtually attending webinars, nothing can replace the value of in-person conferences. I firmly believe our in-person conferences are vital to the continued success of NAHEFFA. We are truly at our best when we gather in-person.

During the conference we welcomed new NAHEFFA Members and Sponsors and sadly we said farewell (until the next time) to a few long-standing NAHEFFA Members and Sponsors that are retiring. We enjoyed great educational sessions, and social events filled with smiles and laughter, all of which confirmed the NAHEFFA community knows how to have a good time!

My hope is the fall conference will serve as a catalyst to jump start and reenergize membership to become more involved and reengaged. Please remain vigilant in your advocacy efforts so our advance refunding and small borrower language is included in the final budget reconciliation bill. Lastly, if you do not already belong, please consider joining a NAHEFFA committee.

Welcome to our Newest NAHEFFA Member!

Welcome to Robert Boyd and the Higher Educational Facilities Financing Authority of Florida (HEFFA). We are so pleased to welcome HEFFA as the newest member of NAHEFFA.

Please enjoy this fall edition of the NAHEFFA Newsletter!

Cheers,

Dennis P. Reilly
NAHEFFA President

In This Issue:

Charles A. Samuels
Washington DC Legislative Advocate
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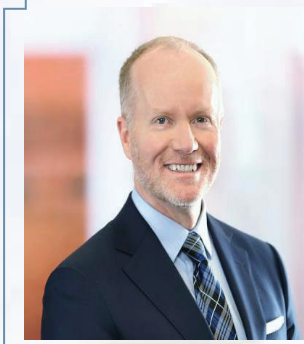
Neal Martin
Senior Director of Government Relations
ML Strategies, LLC



WASHINGTON DC UPDATE

It was a pleasure seeing so many of you at the fall conference in Milwaukee last month. Thanks to Dennis and his team for making it such a success!

Our Washington advocacy panel was scheduled for the final day of the conference and in our presentation we reported on our efforts in support of restoring advance refunding, enhancement of small borrower rules, and language requiring governmental issuers for any new direct subsidy bonds for nonprofits. What we did not know during our presentation was that just hours later, the House Ways and Means Committee would release its language for the proposed $3.5 trillion budget reconciliation bill – the Build Back Better Act (BBB).

The good news is that the committee included our advance refunding and small borrower language. The proposed direct pay bonds do not apply to nonprofits about which many of you may have mixed feelings. Full committee chairman Rep. Richie Neal (D-MA) and select revenue (tax) subcommittee chairman Rep. Mike Thompson (D-CA) have been long-time champions for these provisions and we quickly followed up to thank them and their staff for their support on behalf of NAHEFFA.

The bad news is that, as you're all surely aware, the BBB has run into a wall with Sens. Joe Manchin (D-WV) and Kyrsten Sinema (D-AZ) who have taken issue with the size and scope of the proposal. Sen. Manchin has said he will not support a bill larger than $1.5 trillion, while Sen. Sinema has not indicated what her threshold is for support. Speaker Nancy Pelosi (D-CA), with the support of Senate Majority Leader Chuck Schumer (D-NY) and President Biden, had sought to link passage of the BBB with passage of the $1.2 trillion Infrastructure Investment and Jobs Act, better known as the Bipartisan Infrastructure Framework (BIF). That bill has already passed the Senate in a bipartisan vote of 69-30, but has stalled in the House of Representatives as progressives say they won't support it without action on the BBB.

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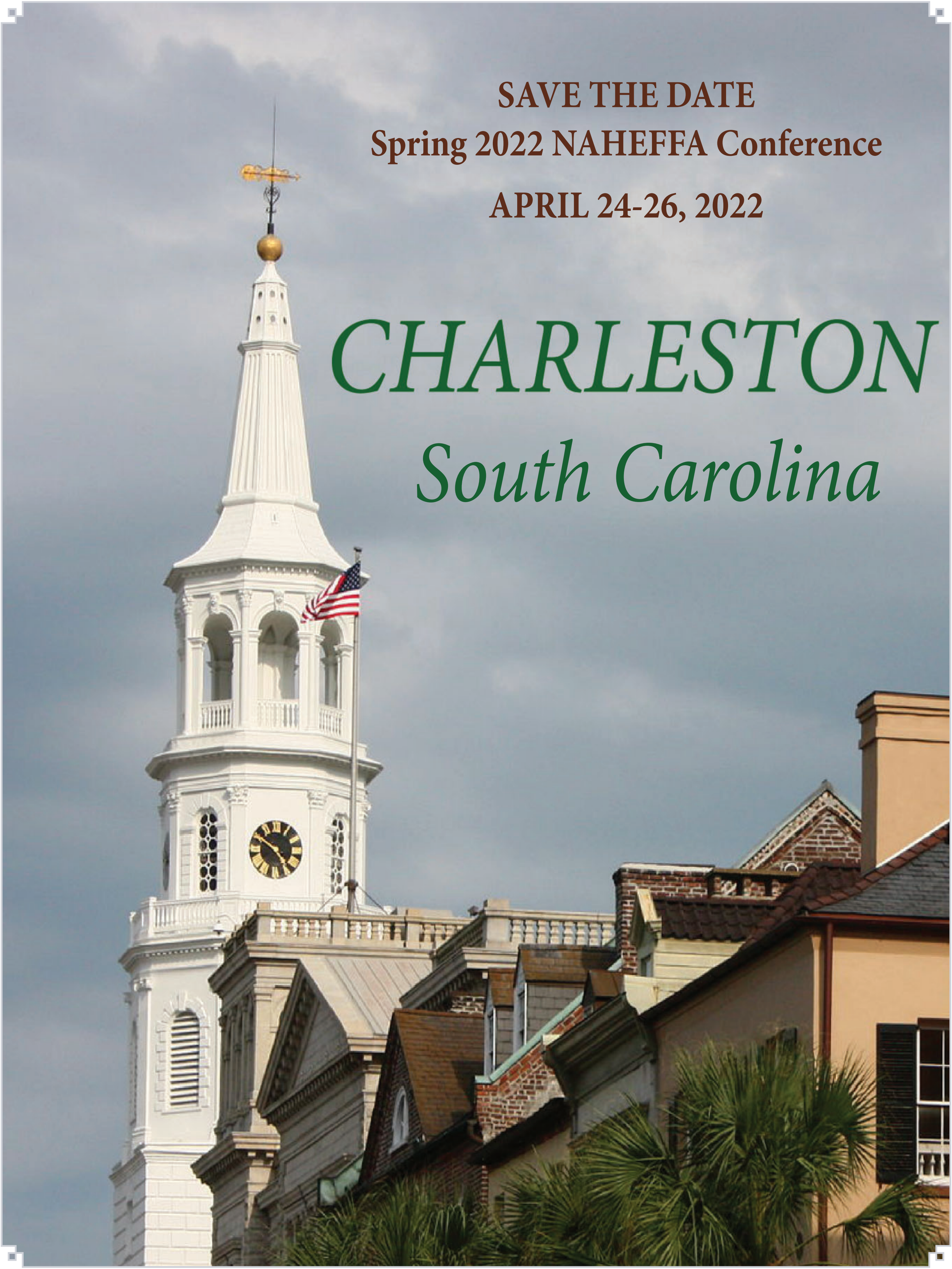
SAVE THE DATE
Spring 2022 NAHEFFA Conference
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South Carolina

Washington DC Update, *continued from page 3*

The bottom line for NAHEFFA is that we have a new deadline of October 31 for action as House, Senate, and White House negotiators seek a compromise on a smaller BBB. The sense on Capitol Hill is that the final price tag, assuming the bill can cross the finish line, will be in the range of $1.9 trillion to $2.3 trillion. What does this mean for our provisions? Unfortunately, it means that we are on the list – along with practically every other provision – for being excluded from the final bill as negotiators seek ways to make a dramatic reduction in the cost of the bill. Alternatively, AR and small borrowers could pass with a “haircut,” such as not being permanent, lasting only a few years unless extended, starting late, or cap limited. Bad news for us would be if only direct pay passes and not the other two.

While we were thrilled with our inclusion in the House committee language, we have cautioned that there was still significant work to do to ensure that the language was supported by the Senate Finance Committee and included in the final language. That dynamic remains, but our lift is a bit heavier as we compete with other provisions for the final smaller bill. If we want to look on the bright side, the stalemate and delay of action on the bill until late October gives us additional weeks to continue making our case for advance refunding and small borrower.

We will continue to be vocal here in Washington on behalf of NAHEFFA, but strongly encourage members to reach out NOW to your congressional delegation urging that the final reconciliation agreement include the House Ways and Means Committee language for advance refunding and small borrower.

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The Nonprofit Real Estate Foundation Alternative to Traditional Leases

By: Nessy Shems, Managing Director, Piper Sandler & Co. and
Jeffrey Fivecoat, Managing Director, Piper Sandler & Co.

Now that most organizations must report operating leases as liabilities on their balance sheets, they have shifted their focus to the impact that these leases have on their financial covenants. As finance staff members dig through their lease documents, often times they are finding (or re-remembering) unfavorable renewal terms and purchase options, or high rent escalators.

As these leases come up for renewal, or if organizations are looking to unlock some of their real estate value, organizations may wish to consider an alternative lease structure that more closely aligns with their not-for-profit goals rather than the more traditional developer-driven lease structures. These will apply to a wide variety of nonprofit organizations, including higher education and healthcare organizations, but for ease of this discussion, we'll focus on a healthcare organization for our examples below.

Consider the typical developer-owned build-to-suit capital lease. Under that structure, a healthcare system would enter into a 10-15 year lease with a developer for a property—say, a medical office building ("MOB")—and, in many cases, the lease would be tied to the developer's cost of capital plus a spread, and would include lease rate escalators. Most leases are structured as triple net, meaning that, in this example, the healthcare system would be responsible for paying the operating expenses of the MOB, including real estate taxes, property insurance, and utilities. In addition, the future accretive value of the MOB, based on the lease rate at time of sale, would accrue to the developer under the typical purchase option included in the lease.

A lower cost alternative can be achieved by entering into a lease with a Nonprofit Real Estate Foundation ("Foundation(s)"). These Foundations were formed in the late 1980s and early 1990s in reaction to the 1986 tax law changes, and maintain a charitable purpose to provide lower cost real estate solutions to further their mission of sponsoring nonprofit charitable organizations. Foundation lease structures have been used to acquire and construct medical office buildings, free-standing emergency departments, administrative office buildings, labs, classrooms, dorms, and other facilities for healthcare and higher education clients around the country. And, because these Foundations are nonprofit, they typically offer more competitive leases than REITs or developers.

In a typical Foundation lease, the Foundation would serve as the owner of the leased facility (in our example a MOB) and would obtain tax-exempt financing based on the credit profile and lease terms of the underlying nonprofit lessor/tenant. For the lessee/tenant, lease payments are based on the Foundation's cost of capital plus an annual Foundation administrative fee, which is typically lower than the spread a for-profit developer would add to their cost of capital. Because of the Foundation's ability to borrow on a tax-exempt basis—via a conduit issuer—lease payments are typically lower than leases offered by developers and other for-profit alternatives. In addition, many of these leases are not secured with a note under the Master Trust Indenture ("MTI"), meaning the lease won't impinge on the organization's debt capacity

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Congratulations to Ruth Keeth and John Sager of the Idaho Health Facilities Authority on their Retirement

The Board of Directors and Members of NAHEFFA would like to congratulate John Sager on his pending retirement as Executive Director of the Idaho Health Facilities Authority. John began his full duties as Executive Director in 2018 and previously was Chief Financial Officer at the Idaho Housing and Finance Association for over 20 years. He has over 40 years of experience in financial management, bond issuance, banking, and asset/liability management for public entities.

NAHEFFA would also like to acknowledge Ruth Keeth on her retirement as a Board Member for the Idaho Health Facilities Authority. Ruth served on the Board for 29 years and brought her wealth of knowledge from her many years of working in corporate trust and tax-exempt financing. During her time as a Board Member of the Idaho Authority, Ruth also served on the Board of NAHEFFA.

We all thank both John and Ruth for the many years of shared knowledge and wonderful memories. We wish you both new adventures and much needed relaxation!

Get Involved! Join a NAHEFFA Committee!
(e-mail info@naheffa.com)

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under its additional debt covenants.

Here's a more specific example: A healthcare system in the Midwest wishes to construct a new freestanding ER and outpatient facility and does not wish to finance it directly (it may have other capital market needs or it simply can't issue debt for the project under its MTI). Under the Foundation lease structure, the healthcare system would select a construction firm to construct the project, and upon completion would sell it to the Foundation which finances the acquisition with tax-exempt bonds sold via a private placement. The Foundation leases the MOB to the healthcare system under a triple net lease for the elected lease term. While the healthcare system would be responsible for paying the typical expenses of operating the MOB, in many cases it would not be subject to real estate taxes—a big savings.

At the end of the term, the healthcare system can elect to either renew the lease with the Foundation on mutually agreeable terms, purchase the MOB for not less than the outstanding lease balance (which is tied to the underlying debt), or return the property to the Foundation subject to a residual value guarantee equal to the outstanding lease balance.

Under the Foundation lease structure, the healthcare system could realize the following benefits:

- A lower cost lease;
- Annual property tax savings (available in some states);
- Long-term operational control and economic benefits of the facilities retained by the healthcare system;
- Flexible lease terms and flexible purchase options: Lease terms can be structured to meet the underlying tenant's preferred accounting treatment and purchase options are generally more favorable than those offered by for-profit developers or real estate investment trusts ("REITs");
- Ability to capture increases in the future value of the MOB;
- Option to purchase the leased property for the cost of the Foundation's remaining debt;
- Won't affect debt service coverage ratio covenants; and
- Potential to eliminate sales tax on construction materials.

Foundation lease terms range from 10-30 years, depending on the goals and objective of the lessor. For example, shorter lease terms may be structured to receive more favorable accounting treatment and can generally lessen the balance sheet impact when compared to traditional ownership or private developer structures.

Based on the health system's credit profile, the Foundation lease structure may require an equity contribution of 5-10%, and lease payments are typically sized to generate debt service coverage of 1.05x until a reserve fund of approximately one-half of annual lease payments is built up. For higher quality credits, 100% loan-to-value and 1.00x debt service can be accommodated.

The Foundation lease structure can be a cheaper form of financing given the ability of the parties to structure lease transactions in a manner that reduces the cost compared to developer-driven financing, and the ability to tailor the transaction terms, covenants, and restrictions while preserving the lessor's capital and credit capacity.

Organizations should consider a wide variety of financing structures (such as direct debt, leasing, and the Foundation lease structure) as a part of their real-estate and finance process or making decisions around the lease renewal of their fully-leased outpatient care, administration, support buildings, and or joint venture facilities.

If any of your conduit borrowers are looking for opportunities to purchase leased buildings, or unlock the value tied up in their real estate portfolio, we'd be happy to help them consider their capital alternatives.

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Welcome to our Newest NAHEFFA Members:

Patrick Ray and the
Arizona Industrial Development Authority
- AND -
Robert Boyd and the
Higher Educational Facilities Financing Authority of Florida.

You can use the following template to reach out to offices:

I am writing to you as ENTER TITLE of ENTER ORGANIZATION.

ENTER SHORT DESCRIPTION OF YOUR ORGANIZATION.

As Congress advances the budget reconciliation bill, we were pleased to see the House Ways & Means Committee include two top tax-exempt municipal bond policy priorities in the recently approved tax provisions for the Build Back Better Act. Specifically, we were pleased to see the inclusion of language that restores advance refunding (Sec. 135102) and language to modify the small issuer exception to tax-exempt interest expense allocations for bond financing (Sec. 135103). Both of these common sense provisions have bipartisan support and we hope that you will communicate your support to leadership for their inclusion in the final legislation.

PERHAPS SHARE SOME BACKGROUND ON HOW YOUR ORGANIZATION BENEFITS THE STATE.

Thanks you for your consideration, and please let us know if we can answer any questions.

If you need help locating contact information for your congressional offices, please reach out to Neal Martin at RNMartin@mlstrategies.com. He will be very happy to hear from you.

Returning to the BIF, we note that it does include some bond-related provisions that may be of interest to some NAHEFFA members. The BIF expands eligible private activity bond projects to include broadband infrastructure, and supports middle-mile deployment efforts. It also provides $600 million for states to issue private activity bonds to finance broadband deployment, specifically for projects in rural areas where a majority of households do not have access to broadband. The bill includes $500 million for surface transportation private activity bonds, increasing the current cap on these bonds from $15 billion to $30 billion. It also allows carbon capture and direct air capture (DAC) technologies to be eligible for private activity bond financing.

NAHEFFA Focus

The Association promotes the common interests of organizations which have the authority to provide capital financing for not-for-profit healthcare and higher education institutions and facilitates national advocacy, support, networking and education on behalf of its members. NAHEFFA focuses its efforts on issues which directly influence the availability of, or access to, tax exempt financing for healthcare and higher educational institutions.

JUST FOR FUN!!!

Word Search!!!

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