Request for City Council Committee Action from the Department of Finance

Date: March 20, 2008
To: Transportation and Public Works Committee
Referral to: Ways & Means/Budget Committee

Subject: Capital Project Reprogramming and Funding of Bike Projects

Recommendation:

1. Amend the City's Financial Policies to clarify priorities for reprogramming capital resources.
2. Receive and file information related to improving flexibility for funding bike or other small capital projects.
3. Approve the attached resolution increasing the City's official "IRS Intent to Reimburse" resolutions for 2008 and prior Capital Improvement Programs up to 125% of estimated project costs and amend the City's financial policies accordingly.

Previous Directives: December 17, 2007 Staff Direction on the Midtown Greenway Bicycle Station:

a) Direct Finance Dept to report back to the T&PW and W&M Committees on the city's financial policy addressing the reallocation of capital project funds from incomplete projects and with suggestions for more flexibility; and

b) Direct Public Works to work with the Finance Department to identify funding and clarify criteria for use of bond financing for bike projects that have a shorter than five year life cycle and report back to the T&PW Committee.

Prepared by: Heather Johnston, Director, Management and Budget; Mike Abeln, Director, Capital and Debt Management
Approved by: Patrick P. Born, CFO and Steven Bosacker, City Coordinator
Presenters in Committee: Heather Johnston, Director, Management and Budget; Mike Abeln, Director, Capital and Debt Management

Reviews

- Permanent Review Committee (PRC): Approval ___ Date ________________
- Civil Rights Approval Approval ___ Date ________________
- Policy Review Group (PRG): Approval ___ Date ________________

Financial Impact

- No financial impact

- Action requires an appropriation increase to the ___ Capital Budget or ___ Operating Budget
- Action provides increased revenue for appropriation increase
- Action requires use of contingency or reserves
- Action is within the Business Plan
- Action requires a change to the Business Plan
- Other financial impact
- Request provided to the Finance Department when provided to the Committee Coordinator

Community Impact
- Neighborhood Notification
- City Goals
- Comprehensive Plan
- Zoning Code
- Other

Supporting Information

The following information is provided in response to the staff direction of December 17, 2007.

Recommendation #1:

Amend the City's Financial Policies to include the following the language:

Reallocation of Capital Resources. *City staff should ensure the timely closeout of capital projects consistent with the guidelines established with State and Federal law. To avoid potential arbitrage penalties, bond proceeds must be spent within two years from the date of bond issuance; if not spent within three years of issuance, special investment provisions must be undertaken to restrict the investment yield. At the time of project closing or abandonment, excess bond proceeds will be reallocated according to the following priorities:*
1. *completed projects with existing deficits to the extent allowable by Federal law and previous Council actions.*
2. *approved projects currently under construction or recurring capital programs with projected deficits within three years of the bond issuance date.*
3. *increased capacity for new bond-funded capital programming through returning the allocations to the debt service fund to pay principal and interest for future projects.*

Reallocations of bond proceeds must follow applicable charter and statutory provisions related to the issuance of bonds and use of bond proceeds consistent with the City's comprehensive plan. New capital projects will be funded through the increased capacity provided by priority #3 by going through the City's five-year Capital Improvement Process.

The combination of increasing future capacity and timely closeout of existing capital projects should provide needed flexibility for new capital projects.

Recommendation #2:

The City's debt is issued consistent with State Statutes and the City Charter and must allow for compliance with IRS regulations governing the use of tax-exempt bonds. The City's current financial policies state:

"***Bond Term***. The City shall issue bonds with terms no longer than the economic useful life of the project...."

Currently, the projected useful life of a bike path project is 30 years and a permanent paving striping project is 2-4 years. Generally, the City issues capital bonds for the bike program in conjunction with other types of capital projects, with most bonds having no longer than a five-year term. The funding of a bike project with net debt bonds is allowable under the existing financial policies.

Finance Department Option for flexible funding of bike or other small projects:

Reallocation of excess bond proceeds or reallocation of authorized but not yet issued bonds requires compliance with State statutes, City Charter provisions and IRS regulations. An option that would improve flexibility for future reallocation of excess project funds would be to fund certain capital projects such as bike projects or other small capital projects with permanent improvement tax levy dollars.

To provide permanent improvement tax levy dollars and maintain the same amount of resources to the capital program, the City would need to reduce the bond redemption levy, which reduces the capacity for other projects financed through net debt bonds. While using permanent improvement levy dollars would require a bit more administrative effort in developing the capital program and determining the tax levies, it would decrease the administrative effort and improve flexibility for closing projects and reallocating excess project funds.

Recommendation #3:

In reviewing bond use provisions, City staff determined that flexibility for using tax exempt bonds to reimburse construction expenditures could be improved by modifying our financial policies to allow for tax exempt bond reimbursement of up to an additional 25% of the original budgeted project cost at the time our capital budget resolution is passed. The recommended policy change will not remove the requirement for departments to request City Council approval for appropriation increases for projects but will simply create additional capacity to reimburse project costs with additional bond proceeds should the need arise due to cost overruns or other factors.

The City's financial policies will also be amended accordingly to create this flexibility with the following language:

> *The City Council expresses its official declaration that pursuant to the IRS Treasury Regulations Sections 1.150-2, the bonding amount to support the reimbursement of expenditures shall be the bonding amount expressed in the Capital appropriation resolution plus an additional 25% of the project's total appropriation.*

The financial policies should also be reviewed to ensure that all funding sources for capital projects are addressed. These changes do NOT impact the appropriation for a capital project. Additional Council action would be required for reallocation of bond proceeds. Attached is a resolution to implement this change for the Adopted 2008 Capital Program and to amend the reimbursement resolution intent for the prior bonding resolutions.

RESOLUTION 2008R-____

By Colvin Roy and Ostrow

This resolution constitutes an official declaration pursuant to IRS Treasury Regulations section 1.150-2 that the City intends to reimburse expenditures which may be made for those projects designated in adopted City Council Resolutions 2008R-065; 2007R-646 through 2007R-651; 2006R-612 through 2006R-617; 2005R-659 through 2005R-665; 2004R-581 through 2004R-587 designated to be funded in whole or in part with bond proceeds by incurring tax exempt debt of the City.

Whereas, the City of Minneapolis is governed by IRS Treasury Regulations section 1.150-2 for reimbursements made with the proceeds of tax-exempt bonds for capital projects; and

Whereas, the City of Minneapolis would increase administrative flexibility by modifying resolutions for those projects designated in adopted City Council Resolutions 2008R-065; 2007R-646 through 2007R-651; 2006R-612 through 2006R-617; 2005R-659 through 2005R-665; 2004R-581 through 2004R-587 designated to be funded in whole or in part with bond proceeds by incurring tax exempt debt of the City; and Whereas, the City of Minneapolis acknowledges the timing between the establishment of project budgets in February and official budget adopted in December for the Capital Budget of the following year necessitates the establishment of a mechanism for adjustments to reflect the actual costs incurred during the construction cycle and to finalize the accounting for the projects; and

Whereas, the City of Minneapolis will continue to govern appropriation changes through separate official actions;

Now, Therefore, Be It Resolved by The City Council of The City of Minneapolis:

That the City of Minneapolis amends the resolutions described above to include the following:

This resolution constitutes an official declaration pursuant to Section 1.150-2 of the Treasury Regulations promulgated under the Internal Revenue Code of 1986, as amended that the City intends to reimburse expenditures which may be made for the projects designated herein to be funded with the proceeds of tax-exempt debt issued by the City. The City intends to reimburse itself for expenditures for each project described herein in an amount of up to 125% of the project cost noted (to take into account the possible increases in actual project costs that may occur due to the timing lag between the budget preparation and the dates of the actual expenditures for project costs). The expenditures to be reimbursed include all preliminary expenses for planning, design, legal, consulting services and staff costs reasonably allocated to the project as well as costs incurred and paid for the design and construction of the projects after approval of the capital budget. The Finance Officer is authorized to make further declarations of official reimbursement intent in connection with the projects described herein consistent with budgetary and financial circumstances.