Tax Supported
New Issue

Kansas Development Finance Authority

Rating

Kansas Board of Regents
(Comprehensive Rehabilitation
Repair Project) Revenue Bonds ...... AA–

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New Issue Details

Kansas Board of Regents-Comprehensive Rehabilitation and Repair Project Revenue Bonds, $31,145,000 Series 2001F, are scheduled to be offered on or about April 17 by negotiation through a syndicate led by George K. Baum & Company. The bonds are due Oct. 1, 2001–2011 with call provisions to be determined.

Security: The bonds are special, limited obligations of the Kansas Development Finance Authority payable solely from and secured by a pledge of the trust estate, which consists of funds appropriated by the State of Kansas. The appropriation is expected to be made from the educational building fund, which receives the proceeds of a one-mill ad valorem tax levied on all tangible property in the State of Kansas.

■ Outlook

Kansas Development Finance Authority (KDFA) is issuing revenue bonds for the Kansas Board of Regents, the governing body of the state's institutions of higher education. Bond proceeds will be applied primarily toward the advanced refunding of outstanding parity bonds and a small portion for capital projects. Security for the bonds consists of appropriations to be made by the state into the educational building fund. The fund receives the yield of a one-mill statewide ad valorem tax; it is expected that this will be the source of the appropriation, although other state sources could be used. While the tax is levied specifically for higher education pursuant to statute, all state moneys require appropriation.

The tax has been levied since 1941 and the current rate was set in 1984. The yield of the tax has increased annually for the past decade; in 1999–2000, the yield amounted to $21.65 million, providing satisfactory coverage for the annual limit of $15 million in debt service. The bonds are issued on parity with outstanding series issued in 1996 and 1997 and are well secured by the level of the one-mill tax collections, as well as by the state's ability to appropriate moneys from other sources to finance needed improvements to the state's system of higher education.

■ Ratings Considerations

The Kansas Board of Regents controls and supervises the state's institutions of higher education. While individual institutions have revenue bonds outstanding, the bonds issued for the current program are the only systemwide debt. Needs were evaluated in 1994 and projects totaling $288 million were identified. Bonding would provide about $164 million and is limited to the amount that can be serviced by $15 million annually. The debt service limit has effectively limited new money issuance to approximately $160 million including the new money portion of this issue. Most of this issue will be applied towards the advance refunding of $29,235,000 outstanding series 1996K bonds, with the $1.0 million balance of net proceeds applied to construction projects. Following this issuance and refunding of outstanding bonds, approximately $128 million in bonds will remain outstanding.

In a broad sense, these revenue bonds are appropriation bonds in that the state may appropriate from any source and that an appropriation must be in place for any state money to be disbursed. However, they also have characteristics of a special tax bond, as the program is designed to be funded from the educational building fund that receives the proceeds of a one-mill ad valorem tax; the tax is statutorily levied for the fund, but appropriation is still necessary. The yield of the tax has grown annually for at least the past decade, and consistent growth is projected at least through the 10-year remaining life of the bonds.

In 1999–2000, the educational building fund received $21.65 million, which provides 1.44 times (x) coverage for the $15 million debt service maximum level that occurs beginning in fiscal 1999 and thereafter. The timing of the receipt of funds is not a problem, as statute provides that 95% of prior year's collections and 100% of the debt service appropriation be deposited on July 1. Coverage of 1.20x for maximum annual debt service is required for additional bonds. The importance of higher education, the stable revenue source, and the good margin of protection provided by the additional bonds test all contribute to the rating levels.

The State of Kansas has no general obligation debt and very little general-purpose debt. The Department of Transportation has $791 million highway revenue bonds outstanding (rated 'AA' by Fitch), which account for the bulk of state-supported debt of about $1.4 billion. Accordingly, debt ratios are low to moderate. The general fund carries a relatively high balance, targeted at 7.5% of expenditures. Sales and income taxes are about of equal importance, accounting for about 39% and 45% respectively of general fund revenue. While the Kansas economy continues to have a significant agricultural component, employment is largely in trade, services, government, and manufacturing. Employment has increased at good rates in recent years and the unemployment rate historically is low. Personal income per capita is somewhat below the national level, and the importance of agriculture contributes some volatility.

■ Strengths

- Expected appropriation source is stable.
- Favorable timing for educational building fund deposit.
- Good coverage margin.
- Kansas has low debt and satisfactory finances.

■ Risks

- Normal appropriation risk.
- Funding base not under control of board or KDFA.

■ Security for the Bonds

The bonds are special, limited obligations of KDFA, payable solely from and secured by state appropriations that are deposited into the revenue fund. The appropriations are expected to be made from the educational building fund, which receives the proceeds of a one-mill ad valorem tax levied on all tangible property in the State of Kansas. However, the levy is not pledged, and there is nothing to preclude the state from appropriating from another source. The bonds are limited to the amount that can be serviced from $15 million annually, ($14 million in fiscal 1997–1998) and additional bonds require that maximum annual debt service be covered 1.20x by fund revenues. The fiscal 1998 appropriation provided for debt service due on a series 1996K-1 note issue, which matured on Oct. 1, 1997.

Appropriations from the fund for debt service have been made through 2000–2001. No additional debt is projected as the full $15 million annual debt service authorization is fully utilized through 2001. The refunding issue reduces annual debt service freeing up capacity to utilize the $1 million in proceeds for capital construction.

The bonds are being issued pursuant to a board resolution and a KDFA bond resolution. In addition, the board and KDFA have entered into a pledge of revenues agreement. Pursuant to the resolution, the trust estate is pledged to the payment of principal and interest, and a principal and interest account is created. Under the pledge of revenues agreement, the board covenants to request an appropriation from the educational building fund or other source for debt service and pledges the revenues received to KDFA. The agreement provides for additional bonds as long as a debt service coverage test of 1.20x is met and there is no default. The test is based either on the most recently completed fiscal year or, prospectively by a consultant, for the next two fiscal years. If coverage is more than 1.50x, no consultant is required.

Over the past decade, revenues to the educational building fund have increased at an average annual rate of about 4.4%, reaching $21.65 million in 1999–2000. Property base growth was especially strong in 1997 and 1998 owing to both healthy increases in new construction and valuations. Revenues rise 5.2% in 2000–2001 and are estimated to increase 5.4% in 2001–2002 based on assessments already undertaken, according to the state. For the next three years, projected growth ranges from 4.8% declining to 4.0%.

The fund carried a year-end balance of about $10 million in 1998–1999, increasing to over $13 million at the end of 1999–2000. Revenues are projected to increase more than 5% in 2000–2001; however, expenditures increase by over 50%, dropping the balance to a projected $6.7 million. The governor's proposed budget would maintain the balance over $6.2 million by the end of fiscal 2001–2002, by reducing expenditures by about 16% with revenue growth of 4.6%. Expenditure projections beyond 2001–2002 reflect only the $15 million in annual debt service and therefore fund balances are projected to increase again. Statute provides that 95% of prior year's collections be deposited on July 1. Thus, there is no reserve for the bonds.

Based on the $15 million appropriation for debt service in 1999–2000, coverage is 1.44x by actual 2000–2001 revenues and 1.52x based on 2000–2001 estimated revenues. In 2001–2002, estimated coverage would be 1.60x. Since the debt service appropriation is fixed, coverage is estimated to rise in line with expected higher property values. The entire debt service appropriation will be fully utilized in each of the permitted 15 years from original issuance in 1996, as anything unused would revert to the fund at fiscal year end.

The Board of Regents governs the state's institutions of higher education, including Emporia State University, Fort Hays State University, Kansas State University, Kansas State University-Salina, Pittsburgh State University, Wichita State University, the University of Kansas, and the University of Kansas Medical Center. The board was reconstituted in 1999 and consists of nine regents appointed by the governor. Not more than five regents may be of the same political party. The improvements being financed by the bonding program are broadly spread among the institutions. The universities in total have $100.28 million in separately secured revenue bonds. KDFA is an independent instrumentality of the state that finances capital improvements and improves access to financing for both governmental bodies and the private sector.

■ State of Kansas

The State of Kansas has a population of about 2.68 million. Population growth has been moderate, increasing 8.5% in the 1990s following just under 5% growth in the 1980s. While agriculture remains an important component of the economy, employment is centered on services and trade, accounting for about 26% and 24% respectively, government (mostly state and local) 18%, and manufacturing 16%. Manufacturing is quite concentrated, with transportation equipment constituting 28% (within that category, aircraft alone is 23%), machinery 15%, and food 16%. Printing and publishing and the meat industry are also significant. Employment growth has been moderate at 2.2% and 1.8% in 1999 and 2000 respectively, slowing from the 3.5% pace in 1998. In 2000, employment growth of 1.8% was led by construction at 6.6%, services 2.8%, government 1.9%, finance, insurance, and real estate 1.4%, and trade 1.3%; manufacturing declined 0.8%. Kansas traditionally has a low unemployment rate, at 3.4% in 2000. The personal income trend is somewhat volatile because of the farm component. In 1999, state growth was 93% of the nation. In 2000, personal income per capita amounted to $26,824, or 94% of the U.S. figure, ranking the state 27th.

Kansas has no general obligation debt. There are relatively small amounts of bonds, mostly issued by KDFA, for such purposes as corrections and buildings, but the only significant debt is that of the Department of Transportation for highway purposes, at $791 million. Total debt attributable to the state is about $1.4 billion, or about $531 per capita and 2.0% of personal income. Significant issuance for transportation is planned including $350 million in 2000–2001 and $320 million in 2001–2002 as indicated in the proposed budget. Upon such issuance debt rations will remain moderate.

The general fund is the state's principal operating account. Major revenue sources are the income and sales taxes, each accounting for about 45% and 39% respectively. Education is the largest item of expenditure. Revenue declined 1.1% in 1998–1999 as a result of a large tax reduction package, while expenditures grew by over 10%, reducing fund balance, which still remained large at $540 million, or 13.5% of revenues. Revenues increased by 5.6% in 1999–2000 and expenditures by 4.1% resulting in a smaller $165 million reduction in fund balance to $378 million or nearly 9% of revenues. The governor's budget estimates revenue growth of 6.7% in 2000–2001 and a restrained expenditure increase of 1.5%, with an ending fund balance of about $430 million. The general fund typically carries a large balance, partly for cash flow purposes. The target level is 7.5% of expenditures. The governor's recommended budget projected revenue growth of 2.2% for 2001–2002 and expenditures of 5.1%, reducing fund balance to about $350 million, which is at the 7.5% target. Recently, revenue projections have been revised downward by $185 million over the next 15 months. Reportedly, the legislature will return from recess at the end of the month to address the projected shortfall.