

Structured Financing For Public Facilities

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Public institutions throughout the United States – such as school systems and hospitals – today face several converging issues, all of which have the potential of placing great financial demands on state governments and, consequently, on taxpayers. These concerns are particularly urgent with regard to institutions of higher education.

Record growths in enrollments have created corresponding needs for all manner of facilities, especially ancillary buildings such as student housing, parking structures, recreation centers and student centers. These expanding needs are frequently coupled with extensive backlogs of deferred maintenance and required upgrades on existing buildings, which are often antiquated and lack desirable features and amenities. Additionally, these ancillary facilities are becoming an important factor in providing the highest quality education, as well as in recruiting and retaining the most desirable students, faculty and staff. Therefore, the long-term success of public institutions depends in part on a state's ability to finance the renovation and expansion of these facilities. That translates into billions of dollars of urgent capital needs over the next 20 years.

Fortunately, the means exist to minimize the financial impact on states and institutions. The renovation and expansion of these facilities can be financed, at least in part and often completely, based on the corresponding cash flows of the needed projects. This type of financing can often be completed using tax-exempt “revenue” bonds, further reducing the obligations on the state while still maintaining the highest levels of institutional control and flexibility.

Unlike traditional “revenue” bonds, however, “structured” financing allows a project to be financed partially or entirely based upon its own financial strengths and merits, with no reliance on the credit of the state. While borrowing costs are slightly more expensive than for ordinary state funds, this burden is absorbed by the project's cash flows and the state itself can incur less direct debt, preserving its credit rating and borrowing capacity and enhancing its overall financial positions. Further, when these projects are developed and owned by non-profit entities affiliated with the institutions (e.g. alumni associations, support organizations) they can be financed with the bondholders looking to the project owner, rather than the state and its taxpayers, for bond repayment. Because this type of financing is “non-recourse” to the state, it generally does not affect the state's financial assets or liabilities.

Another benefit to “structured” financing is that creating the basis for strong and stable financial performance is a prerequisite to development. Fiscal prudence and efficiency are therefore instilled into every step the development process and the ongoing operations. Because the project must stand on its own financially, decisions affecting development costs, project revenues and operating expenses are naturally required to make sound business sense in order to maximize performance. This factor causes institutions to operate in a pragmatic and efficient manner. Unlike the old “big government” methods of undertaking projects depending heavily on if and when the state can allocate taxpayer funds, the “structured” method empowers institutions to finance and develop facilities based on strong, bankable business cases. This market-driven approach presents institutions with an important and valuable tool for responding to the realities of demand, competitions and changing conditions.