National Association of Health and Educational Facilities Finance Authorities

Supporting ACCESS

March 2014

Not a Pretty Picture for Issuers

by Mark Melio, Managing Partner – Melio & Company, LLC

Municipal bond volume was down considerably in 2013. Overall volume fell 12.5% (or by $50 billion) to $334.6 billion. The most significant negative component was a 30% decline in refundings.

Healthcare issuance was down 22.8% last year to $28.8 billion, however, issuance by colleges and universities increased 14.3% to $14.2 billion, mostly in the first half of the year. With interest rates trending higher, we are seeing fewer tax-exempt refundings (mostly restructurings associated with merger and acquisition activity). Negative outlooks by the rating agencies exist for both sectors, and overall municipal volume is projected to decline another 10% in 2014.

There was a notable increase in taxable issuance for healthcare and higher education institutions in 2013. Healthcare taxable issuance more than doubled to $1.8 billion, while higher education issuance increased more than 60% to $4.2 billion. Last year, taxable debt represented 7% of all healthcare and 15% of all higher education issuance. We expect taxable issuance to continue to increase for both sectors going forward. In fact, we have been seeing large institutional investors, primarily insurance companies, approach certain Aa/AA borrowers directly to privately purchase a significant amount of bonds i.e., in excess of $100 million, on a taxable basis. These private placements have 35 – 40 year maturities, as well as make-whole redemption provisions, which are common in the taxable markets.

Private placements, on the whole, are up. Banks now hold over $400 billion of municipal bonds, which is twice the amount they held four years ago. Healthcare private placements – both tax-exempt and taxable – increased to $6.4 billion last year, and represented nearly 25% of total healthcare issuance. While this phenomenon wasn't as dramatic for higher education, there were still $1.8 billion of private placements for colleges and universities last year.

Four banks – Bank of America, JP Morgan Chase, US Bank, and Wells Fargo – have over 50% of the market concentration for healthcare letters of credit and stand-by bond purchase agreements. BB&T, BNYMellon, Northern Trust and PNC total over 15%. Barclays, BMO and TD Bank total about the same. As long-term rates rise, and with short-term rates at unprecedented lows, variable rate demand bonds and other short-term variable rate financing structures have become extremely attractive for healthcare and higher education borrowers.

Banks are clearly compensating for the near obliteration of the auction rate

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2014 NAHEFFA Conferences

March 24-26, 2014
New Orleans, LA
Hilton New Orleans Riverside

September 10-12, 2014
Big Sky, MT
Big Sky Resort

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NAHEFFA President's Message

by Pamela A. Lenane, Vice President and Acting General Counsel
Illinois Finance Authority

Pam Lenane

As I sit here to write my final column as NAHEFFA President, I can't help but think what a great organization NAHEFFA is and what wonderful people are a part of it. I have worked closely with so many of you during my tenure as president and have truly enjoyed the experience. We are a unique organization in a unique niche of the market and we all pull together to make sure our voices are heard. Thank you to the membership, especially the committee members and the Board of Directors for helping me during my presidency. I also want to thank Chuck Samuels for always having an ear open in DC and advocating for our group. It has been a great pleasure to work with you all during my term.

As one of my last pieces of business before my term ends, I would like to remind you all of the conference next week in New Orleans, LA. We have had some bad luck in the past when we have tried to hold it in the Big Easy but this year it is happening. Both the Health Education Authority of Louisiana and the Louisiana Public Facilities Authority have put together a really fascinating group of speakers for what is sure to be another excellent conference. Thank you to Jacob and Debbie from HEAL and Jim and Martin from LPFA for all of your hard work and dedication to making this conference great. Also, thank you to the conference committee who continues to roll out our biannual conferences. As a reminder, conference presentations will be available on the NAHEFFA website ahead of the conference.

The Corporation Meeting scheduled for Tuesday, March 25th will focus on NAHEFFA ByLaw revisions, our FY 2015 Budget and the election of new directors. If you are attending the conference, please plan to be in attendance at the Corporation Meeting. If you are not attending the conference but would like to place an absentee vote, please contact Nichole Doxey at ndoxey@naheffa.com.

It will be great to see you all in New Orleans. ■

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For more conference information and to register, please visit the conference website.

Hosted By:
Health Education Authority of Louisiana
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WASHINGTON REPORT

by Charles A. Samuels, Mintz Levin
General Counsel, NAHEFFA

Chuck Samuels

The year 2014 took off with a roar for NAHEFFA's advocacy program. A leading member of Congress and the President proposed damaging tax law changes and the SEC and MSRB are developing a regulatory regime for financial advisors which may significantly change practices in our conduit structures. The tax proposals probably are not serious threats in the short run but form an agenda for future threats and our advocacy. The securities law issues must be grappled with now and have required development of new policy by the Association.

First, House Ways and Means Committee Chairman Dave Camp of Michigan released a discussion draft of his Tax Reform Act of 2014. It is unlikely that Congress will consider these issues this year but it creates a threshold, list and vehicle for future discussions in the next Congress or next presidency and must be treated seriously. This is particularly the case because many of the proposals, including on tax exempt bonds, may not be far different from those that we could expect from some Democrats, such as new Senate Finance Committee Chairman Ron Wyden of Oregon.

The most direct and threatening proposal is to eliminate future issuance of tax-exempt private activity bonds. Perhaps colored by reports and a congressional hearing regarding certain economic development projects for corporations, the entire category would now be eliminated. Because of the unfortunate connotation of "private activity," there probably is confusion about what constitutes such bonds, which not only include nonprofit health and education and other charitable purposes, but housing, airports and ports. This is illustrated by a comment by an official of the National Governors Association, who indicated that such bond issuances are relatively small and might need to be sacrificed. This official and others must be educated about the size, scope and enormous benefits of this category, particularly with respect to nonprofit bonds. Our national study on the economic implications of losing or limiting the tax exemption is being replicated by several authorities at the state level and all authorities should directly and through their borrowers communicate the importance of this category to the Congress.

Other Camp proposals include a surtax on wealthy taxpayers which would include municipal bond interest, repeal of future advance refundings, elimination of bank qualified bonds - which has been a tremendous advantage for small borrowers-- and eliminating corporate tax incentives for nonbank property and casualty companies which purchase municipal bonds. New issues of tax credit bonds also would be repealed.

President Obama's budget proposes the 28% cap on deductions for high income taxpayers and a new direct pay subsidy program similar to Build America Bonds which could also be issued for short-term working capital and nonprofit entities. The President proposes that these bonds would not be subject to sequestration which has been a problem with the Build America Bonds. Arbitrage restrictions would be eased along with a number of other technical changes, including eliminating entirely the remnants of the 150 million dollar cap on non-hospital 501(c)(3) bonds. There also is a proposal for an independent national infrastructure bank. It is not expected that many, if any, of these proposals will be seriously considered by Congress. The budget proposals, like the Camp draft, can be looked at as political and intellectual capital for the future.

On the securities side, the SEC and MSRB are rolling out the regulatory scheme for municipal financial advisors. First, as reported, the SEC cleared up the threat that authority employees, board members and borrowers might somehow become ensnared as regulated persons. But, this leaves a whole host of questions regarding under what circumstances banks can communicate with clients and potential clients without new registration and regulatory obligations applying and how the rules operate in conduit financing with issuers and borrowers as separate entities.

The MSRB issued a proposed rule, Draft Rule G – 42 on Duties of Non-Solicitor Municipal Advisors, which requested comments, among other issues, on the obligations of financial advisors to obligated parties/

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securities market, and are helping to create the contraction in variable rate demand bonds. However, if proposals by bank regulators are adopted, municipal holdings by banks may not meet liquidity requirements, and may diminish banks' appetite for tax-exempt paper.

Healthcare mergers and acquisitions are continuing at a vigorous rate. The trend has been toward larger scale mergers and the creation of regionally dominant systems. Independent hospitals have become few and far between. The justifiable distractions of this merger-mania as well as the lessening need for inpatient bricks and mortar resulted in a decline in healthcare new money issuance of approximately 12% last year. Healthcare new money issuance is on pace to decline by another 16% this year.

Higher education issuance has slowed as spreads and rates have become less favorable. Managing expense growth relative to revenue growth, heightened competition for students, and reduced federal funding are additional challenges faced by colleges and universities. New money issuance is expected to remain slow.

Besides all that Mrs. Lincoln, I look forward to seeing all of you at the upcoming NAHEFFA conference in New Orleans. If you have any questions or if you would like any more information with regard to this article, please let me know. ■

Washington Report, *continued from page 3*

borrowers and whether the fiduciary duty applies. This proposal prompted NAHEFFA to focus on the structures and benefits of the various, diverse relationships of financial advisors, authorities and borrowers. A special meeting was held in Chicago, hosted by IFA, and numerous authorities provided valuable input on comments which were drafted with the critical assistance of David Kates of Chapman and Cutler. Our comments—which can be found on our website—are supportive of Dodd- Frank's municipal financial advisor provisions and in general support the SEC's regulations and MSRB's proposal. We stressed, however, that as applied to conduit financings, valuable communications which benefit borrowers should not be unduly restricted. Therefore, given the close identity of interest of our authorities and our borrowers, we proposed a regulatory regime under which authority financial advisors could assist borrowers and borrowers' financial advisor communications could continue to benefit issuers. We also made clear the law does not authorize MSRB to impose a fiduciary duty on financial advisor – obligated person/borrower relationships but nonetheless there are substantial duties of care which should apply as we outlined.

In addition, the SEC still needs to clarify a number of aspects of when the financial advisor regulatory requirements kick in so we will be meeting with the Commission to discuss particular conduit issuer- borrower scenarios.

So, there is a lot of activity on both basic policy and technical levels affecting our financings. I hope as many of you as possible will be active within NAHEFFA on these important issues. See you in New Orleans. ■

NAHEFFA NOTES

Mississippi Hospital Equipment and Facilities Authority Says Goodbye to Charles Harrison and Welcomes Richard Grimes as New Executive Director

Charles L. Harrison, Executive Director, Mississippi Hospital Equipment and Facilities Authority (MHEFA), retired effective December 31, 2013. Charles joined the Mississippi Hospital Association in January of 1998 and also assumed the responsibilities of MHA's VP of Capital Programs (MHA holds the management contract on MHEFA). A graduate of Meridian Community College and University of Southern Mississippi, Mr. Harrison also served as CFO at Baptist Health Systems prior to joining MHA/MHEFA.

MHEFA's Chairman Keith Winfield presented Mr. Harrison with a plaque recognizing his years of service of dedication to MHEFA. The Chairman wished him well and stated that he would certainly be missed. At the same time, the MHEFA Board welcomed Richard Grimes as the new executive director stating that his experience will serve him well in the new position.

Richard Grimes fulfilled the executive director position on January 1, 2014. Mr. Grimes, CPA, previously served as Chief Financial Officer, Mississippi Hospital Association. He has been associated with MHA/MHEFA for approximately 10 years and in addition to MHA's CFO and MHEFA Executive Director, he is responsible for the oversight of several financial subsidiaries of MHA. He is a graduate of Mississippi State University and began his career in public accounting prior to joining the MHA staff. ■

To Our Sponsors

Greetings from the NAHEFFA Sponsorship Committee!

The former entities that formed NAHEFFA in 2007 were the NCHFFA (National Council of Health Facilities Finance Authorities) and NAHEFA (National Association of Higher Educational Facilities Authorities. For many years these entities held separate conferences each year until 1994. Waterville Valley, NH was host to the 1st Joint Fall Conference and when we began tracking our conference sponsors. We would like to take this opportunity to recognize the following companies who have supported both of our conferences every year since 1994:

- Bank of America Merrill Lunch
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- Standard & Poor's

On behalf of the member authorities of NAHEFFA, we wish to express our gratitude and thank you for your continued support of our organization. Without this support, NAHEFFA would not be able promote the common interest of the organizations with authority to provide capital financing for health and educational institutions; providers of health or educational services; and Industry organizations supporting and/or representing those providers of health or educational services.

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NAHEFFA Contacts

Nichole Doxey
Operations Director, NAHEFFA
P.O. Box 906
Oakhurst, NJ 07755
(888) 414-5713 p&f
ndoxey@naheffa.com

Charles Samuels
Member, Mintz Levin
701 Pennsylvania Ave NW, #900
Washington, DC 20004
(202) 434-7311 p | (202) 434-7400 f
CASamuels@mintz.com