

# Financing Capital Projects

By Sheila St. Germain

In general, financing should be considered as part of the initial development process of a capital project. Below is a step-by-step process for determining and obtaining the right financing for your project. Of course, a bond counsel attorney should also be hired to review the warrant article for the authorization of bonds and to review the steps required by statute for this process.

## Step One:

As the project is developed, the methods of financing should be considered. The residents may be supporting the project, but at some point they will want to know the cost. The research required will depend on the type of project. For example, many water and sewer projects qualify for the State Revolving Loan Program or programs provided by USDA. These programs provide low rates of interest, but require more research to understand the terms and availability of the funds. If the project may qualify for these special programs, it is worth the research required. If the project does not qualify for special programs, the New Hampshire Municipal Bond Bank (Bond Bank), local banks, the municipality issuing the bonds in the market and capital leases are other alternatives. An estimated amortization schedule of costs over the term of financing and the effect on the tax rate will provide the cost information for the residents. The Bond Bank provides estimated amortization schedules for various amounts and terms to assist municipalities with the financing costs of their projects. This service is provided to all municipalities to assist with the initial phase of the project. There is no requirement to borrow through the Bond Bank to use this service.

## Step Two:

After the project is approved and the bonds are authorized,

it is time to determine the method of financing. A cash flow of expenditures should be created to determine when the bonds should be issued. Some municipalities prefer to borrow temporary funds to start construction and wait to issue the long term financing when they know the exact amount to be expended. If the project will occur over an extended time, the borrowing may be done in phases. In general, funds must be expended within two to three years of receiving the funds, depending on the amount and type of project. There are several laws and IRS regulations pertaining to bonds. Consequently, it is advisable to discuss the timing for the issuance of bonds with bond counsel and financial advisors.

## Step Three:

The application process will vary depending on the financing method. The majority of methods will require a bond counsel opinion and audited financials.

## Step Four:

After the approval process is completed, the bond issuance process begins. If the method chosen was State Revolving Loan, USDA, or a local bank, the financing is not being issued in the market, so the process will include signing documents with the agreed terms. If the Bond Bank or the municipality issuing their own bonds was chosen, the process will involve several steps before the bonds are issued.

Bonds issued through the Bond Bank are issued as part of a pool. The Bond Bank is a quasi-independent state agency. The Bond Bank combines the bond issue requirements from several cities, towns, school districts, village districts and counties into one pooled issue. After the Bond Bank's

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Board has approved the municipality's application, information from the application is used to develop the details for the bond sale. Credit ratings are reviewed and a preliminary offering statement is prepared for the marketing of the bonds. The municipalities participating in the sale will be signing loan agreements and various legal documents from bond counsel. The municipality's bond is issued to the Bond Bank. The combined total from all of the municipalities is sold in the market as New Hampshire Municipal Bond Bank Bonds. All of the participants share the issuance costs and receive the benefit of the Bond Bank's credit in the market. A credit rating for the municipality is not required.

If the municipality decides to issue bonds directly in the market, advisors are hired to assist with this process. The primary advisors are the financial advisor and bond counsel. The municipal officials meet with the advisors to discuss the cash flow required by the projects and develop a plan for the issuance of the bonds. At least one credit rating is required to be able to market the bonds. The financial advisor assists the municipality with the presentation to the credit agency. There will be several conversations between the municipality and the credit rating agency analysts. A preliminary official statement is prepared to provide information about the

terms of the bond issue, the project to be funded, financial information, economic, legal and general information about the municipality. Investment firms send a bid to the financial advisor on the bond sale date. The financial advisor analyzes the bids to determine the lowest interest cost and the bonds are generally awarded to the lowest bidder.

### Step Four:

The bonds have been sold and the funds will be available in a few weeks. The final documents and the bond are prepared by bond counsels. Another round of signing multiple copies of legal documents and then the funds arrive. For several years, the majority of bonds have been sold with premiums. Basically, investors prefer an interest rate on the bonds that is higher than the current yield. They are willing to pay a considerable premium above the par value of the bond. The original bond amount for each municipality is reduced by their allocation of the premium. The municipality receives the full amount requested, but pays back a lower amount of principal. The interest rates will be higher, but the True Interest Cost will reflect the real rate to the municipality because it factors in the premium received by the municipality.

### Step Five:

Time to spend the money! Be sure to track expenditures and interest income earned on funds before expended according to IRS rules.

### Step Six:

Enjoy your new project and make timely debt service payments!

*Sheila St. Germain is Executive Director of the New Hampshire Municipal Bond Bank. Information about the NHMBB is available on their website at [www.nhmbb.org](http://www.nhmbb.org).*

*If you would like additional information about financing alternatives, there will be a session (Municipal Financing Alternatives) at NHMA's Annual Conference on November 16, 2016, at 10:45 a.m. There will be a panel consisting of representatives from Devine Millimet & Branch, PA, the Bond Bank, Municipal Leasing Consultants, PFM Financial Advisory Group, State of NH Revolving Loan Fund and United States Department of Agriculture – Rural Development.*



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