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WRITTEN ONLY

TESTIMONY BY CRAIG K. HIRAI
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
TO THE SENATE COMMITTEE ON HOUSING
ON
HOUSE BILL NO. 869, H.D. 1

**March 16, 2021
1:15 P.M.
Via Videoconference**

RELATING TO SPECIAL PURPOSE REVENUE BONDS TO ASSIST LUANA KAI A
LIFE PLAN COMMUNITY.

The Department of Budget and Finance offers the following comments on House Bill No. 869, H.D. 1, which authorizes the issuance of Special Purpose Revenue Bonds (SPRB) to assist the Luana Kai A Life Plan Community, a Hawaii nonprofit corporation, in the development and operation of a continuing care retirement community pursuant to Part II, Chapter 39A, Hawaii Revised Statutes.

The Department would like to inform the Legislature and prospective SPRB parties that should the legislation be approved, approval of the SPRB issuance and conduit loan will require further review of the financing proposal to ensure compliance with all federal, state and credit underwriting requirements. For additional information, please consult our FAQ located at the following link: <http://budget.hawaii.gov/wp-content/uploads/2012/11/SPRB-FAQ.pdf>.

Thank you for your consideration of our comments.



LUANA KAI – A Life Plan Community

TO: REPRESENTATIVE SYLVIA LUKE, CHAIR
REPRESENTATIVE TY CULLEN, VICE-CHAIR
MEMBERS OF THE HOUSE FINANCE COMMITTEE

RE: TESTIMONY IN **SUPPORT** OF HOUSE BILL (HB) 869
RELATING TO SPECIAL PURPOSE REVENUE BONDS TO ASSIST LUANA KAI A LIFE PLAN
COMMUNITY.

Dear Chair, Vice-Chair and Members of the Committee:

Luana Kai is a nonprofit organization that is set up to be a tax-exempt 501(c)(3) not-for-profit entity. Luana Kai will own a proposed life plan community to be located in Hawaii Kai, Honolulu, Hawaii. Because of its 501(c)(3) status, it will be eligible for tax-exempt municipal bond financing (special purpose revenue bonds) through the State of Hawaii Dept. of Budget and Finance (B&F).

A life plan community is a residential retirement alternative for seniors 62 and older. It is geared to healthy seniors interested in a community lifestyle supporting health and wellness, access to on-campus restaurants and activities, and promotion of a social model of aging. Residents may age through a continuum of care, and one or both members of a household may access assisted living, residential memory care and/or skilled nursing, if needed. Generally, the financial model provides discounted services in levels of care beyond independent living.

Luana Kai in particular is preliminarily planned to include 260 independent living apartments of varying sizes, 40 assisted living apartments, 30 memory care apartments, and 36 private skilled nursing suites. The program would include: housekeeping, dining options, wellness and fitness, security/emergency alert system, scheduled transportation services, and social and recreational programs. Higher levels of care include assistance with activities of daily living (dressing, bathing, toileting, medication management, and feeding) and health care services.

Luana Kai's market study confirms that the Honolulu market, and Hawaii Kai specifically, are underserved and lacking sufficient senior housing options. In fact, US Census data show more citizens age 65 and over in East Honolulu/Hawaii Kai (25.4%) than in the City and County of Honolulu (18.2% on average).¹ Luana Kai will provide housing in an attractive and upscale design, with green spaces and community connections. The developers envision commercial businesses at the ground level open to the neighborhood, including a possible medical clinic,

¹ www.census.gov/quickfacts/fact/table/easthonolulucdphawaii,honolulucountyhawaii/HCN010212h

coffee house, etc. One parking spot will be provided per independent resident along with group transportation, but generally the traffic impact of projects like Luana Kai is much less than a condominium or housing complex of similar size.

Special purpose revenue bonds issued through the State do not impact the State's financial condition, nor put the State at risk of bond repayment, nor put Hawaii citizens at risk of repayment or of higher taxes, nor do they affect the State's bonding capacity for its own infrastructure. See B&F's SPRB-FAQs <https://budget.hawaii.gov/wp-content/uploads/2012/11/SPRB-FAQ.pdf> attached.

The State simply acts as a conduit to confer upon the financing the State's tax-exemption. Current IRS rules prohibit 501(c)(3) entities from accessing the financing market directly without a conduit, even though these entities are tax-exempt otherwise.

Luana Kai respectfully requests support of the necessary legislation permitting the State on behalf of the Corporation to issue special purpose revenue bonds in an amount up to \$500 million. An early tax-exempt financing of approximately \$20-25 million will provide capital for architectural work, development activities and marketing to seniors. This debt will be refinanced under the auspices of the original legislation once the project meets all necessary milestones. The Luana Kai development and financing team have significant experience with life plan communities, and both the investment banker and one of the development partners successfully brought Kahala Nui to the market in 2003.

Thank you for the opportunity to testify

SPECIAL PURPOSE REVENUE BONDS – FREQUENTLY ASKED QUESTIONS

Q: What is a Special Purpose Revenue Bond (SPRB)?

A: Special purpose revenue bonds (SPRBs) are a type of municipal revenue bond authorized by Hawaii's Legislature that can be issued by the State to provide loan financing to assist qualifying private capital improvement projects (for example, certain hospital or school construction) in the public interest. The bonds do not constitute a general obligation of the State and are not State monies. SPRBs are sold to private investors, who provide the actual funds and invest their funds in exchange for tax-exempt or taxable interest payments. The borrowers are required to secure the loans with revenues as part of the loan agreements. For the State, selling SPRBs is a way to facilitate loans for certain categories of private business projects without spending taxpayers' money or placing the State's credit at risk.

Q: How Would SPRB Financing Affect Me and Hawaii?

A: SPRBs that finance loans for improvement projects:

- • are not grants or subsidies to borrowers;
- • are funded by private investors, not by the State of Hawaii;
- • are loans to creditworthy borrowers that must be repaid promptly and with interest;
- • do not affect or jeopardize the State's credit rating;
- • can enable needed improvements on projects that may not be financially feasible otherwise;
- • can support maintenance of critical infrastructure projects that serve and protect the public;
- • are investments funded by private investors seeking tax-exempt interest payments while bearing risk of nonpayment (e.g. loss of their investment); and
- • do not divert public funds from infrastructure, education or other public functions.

Q: How would SPRB financing work?

A: The Legislature authorizes the sale of special purpose revenue bonds (SPRBs) to private investors, and the revenues are used to fund loans to borrowers for improvement projects. Investors receive repayments of principal and tax-exempt interest payments over time from the project owners. Because investors accept lower interest rates for tax-free income, project owners save money.

Q: Is SPRB financing already used to fund projects in Hawaii?

A: Yes. The SPRB funding mechanism has been used for projects with public benefits, including utilities, health care facilities, and certain educational and early childhood education facilities.

Q: How would a borrower/project owner apply for SPRB financing?

The process begins with a borrower securing legislative authorization for the Department of Budget and Finance (B&F) to issue the SPRB. Negotiations between the borrower, B&F, underwriter and trustee regarding the terms of the SPRB issuance follow. The underwriter sells the SPRBs to investors, the investors' money is conveyed to the trustee, and the trustee loans

those proceeds to the borrower. The borrower makes payments of principal and interest to the trustee, who in turn makes payments of principal and interest back to investors.

Q: Would funds for SPRB projects take money directly away from other public works/infrastructure projects?

A: No. Private investors provide the money that is loaned to fund improvement projects, and the borrower repays the principal and interest on the loan. Selling SPRBs enables funds to be loaned for private capital improvement projects serving a public interest without spending taxpayers' money.

Q: Don't tax-exempt bonds mean the State loses out on collecting income tax from investors?

A: Possibly, but not necessarily. Although the tax-exempt status of SPRBs means that the State would not collect income taxes on interest paid to Hawaii SPRB investors, those investors wouldn't necessarily select a Hawaii-based taxable bond alternative if the SPRB wasn't available. The State wouldn't incur a loss on SPRBs sold to out-of-state investors who aren't Hawaii taxpayers.

Q: Would financial need be a consideration in whether the SPRB financing would be made available to particular borrower?

A: No. The SPRB financing mechanism considers the merits of the project, not financial need of the borrower, and the financing mechanism takes the form of lower interest loans, not grants or subsidies.