




Office Memorandum

Date: March 29, 2010

To: Commissioners and Agency Heads
Agency Accounting Coordinators

From: Tom Hanson, Commissioner 

Subject: “After the Bonding Bill” – The Next Steps

This memo gives an overview of key constitutional, statutory and other legal requirements regarding how state agency recipients of state capital appropriations may spend the bonding bill appropriations.

This memo is not an exhaustive reference to all requirements. It summarizes the most noteworthy items and identifies resources for additional information. Agencies should consult with their appropriate financial and legal advisors regarding these and other requirements.

This memo describes requirements associated with:

- 1) Public ownership, public purpose, and use agreements for state-funded projects
- 2) Standard state grant agreements
- 3) Non-state matching requirements for specific projects
- 4) Reimbursing local governments
- 5) Review of grant recipient’s operating program
- 6) Change in fund accounting for some capital projects
- 7) Qualified capital expenditures
- 8) Staff costs for project management
- 9) Sustainable building guidelines for new buildings; alternative energy sources; recycling construction and demolition waste
- 10) Predesign review by the Department of Administration
- 11) Design review by legislative committee chairs
- 12) Up to one percent for art
- 13) Project cancellations

More information on these topics may be found in the Capital Grants Manual at <http://www.mmb.state.mn.us/doc/bonds/grants/grants-manual.pdf>. The memo also references

MAPS operating policies and procedures that apply to capital appropriations. Minnesota Management & Budget (MMB) has posted all MAPS policies and procedures on its web site at <http://www.mmb.state.mn.us/maps-manual>.

1) Public Ownership, Public Purpose, and Use Agreements for State-Funded Projects

The Minnesota Constitution, in Article XI, Section 5, limits the appropriation of state general obligation bonds to state agencies and political subdivisions of the state. Because of this constitutional constraint, grants or loans for capital projects from bond proceeds **cannot** be made directly to non-profit or for-profit organizations.

Minn. Stat. Sec. 16A.695, subdivisions 8 and 9, summarize key requirements of general obligation bond financing. This funding can only be used:

- to finance the acquisition and betterment of **public** lands and buildings and other improvements of a capital nature that are used to **operate a governmental program**; and
- for predesign and design for specifically identified projects that involve the operation of a governmental program or activity.

The same statute provides guidelines that must be followed when a capital project benefits a non-profit or for-profit organization. Generally, for a private organization to benefit from state bond proceeds, the capital project must be owned by a state agency or political subdivision that then enters into a use agreement with a private organization to provide the public program.

A state agency or political subdivision must be more than merely a conduit with a one-time responsibility of passing the bond proceeds through a grant agreement to the private organization. The public entity that enters into a use agreement with the private organization must be an active participant in the public program, and it must also have ongoing oversight of the program. **The Commissioner of MMB must approve all use agreements for bond-financed property.**

The Commissioner of MMB's *Second Order Amending Order of Commissioner of Finance Relating to Use and Sale of State Bond Financed Property* dated March 9, 2010 (the "Commissioner's Order") includes more detail on the requirements that apply to bond-financed property, including property that is used by a non-public party. (This document is posted online at <http://www.mmb.state.mn.us/doc/bonds/history/order.pdf>.) Agency accounting coordinators should review MAPS operating policies 0302-01, 0302-02, 0302-03 and 0302-04 when preparing Appropriation Entry (AP) forms for a capital appropriation that benefits a non-profit or for-profit organization. Agencies may also wish to consult with their Attorney General's staff regarding the various legal requirements affecting state capital appropriations that benefit a non-public entity.

The MMB contacts for Minn. Stat. Sec. 16A.695 issues are Kathy Kardell, kathy.kardell@state.mn.us, (651) 201-8030, and Gay Cerney, gay.cerney@state.mn.us, (651) 201-8049.

2) Standard State Grant Agreements

All general obligation capital grant agreements must describe how bond financing will be used, identify the public program to be operated on bond-financed property, and otherwise ensure that the provisions imposed by Minn. Stat. Sec. 16A.695 are implemented. The Attorney General's office, in cooperation with MMB, has developed standard grant agreements for state agencies to use when providing capital grants.¹ These grant agreements contain provisions covering a wide variety of applicable statutory and constitutional requirements. Standard grant agreements for bond-financed and general fund cash-financed projects are posted on MMB's website and can also be obtained from the Attorney General's office. (For grant agreement documents that apply to bond-financed projects, see <http://www.mmb.state.mn.us/bond-grant-info>).

There are two basic versions of the state grant agreements – construction grants and end grants. Construction grants provide periodic reimbursement to the grantee during project construction. A construction grant agreement will have performance bonds and a fixed price contract. The state agency, as grantor, approves the project budget, receives invoices, and makes payments of state funds to the grantee, no more often than monthly. Final payment information must include a certificate of occupancy. There is a third version of state grant agreement which is used when the grant will fund the predesign and/or design phase only of a project.

End grants reimburse the grantee after the project has been completed. The grantee assumes full responsibility for completing the project, including providing up-front financing as needed to see the project through to completion. The state agency pays out the state appropriation for the project once the project is complete and a certificate of occupancy has been obtained.

MMB recommends that agencies use end grants whenever possible. However, agencies will need to meet with grantees and consider the dynamics of each project when deciding which grant agreement is best to use.

The state cannot advance funds to grantees prior to a signed grant agreement under any circumstances. Funds will be disbursed only when a grant agreement is signed and project costs have been incurred. No funds will be disbursed prior to the start of the project.

The Commissioner's Order requires that a declaration be recorded against real estate that is purchased or improved with state general obligation bond proceeds. MMB now requires agencies to send a photocopy of each recorded declaration to Angie Weidell-LaBathe of MMB, (651) 201-8086, angela.weidell@state.mn.us.

¹ A state agency can choose to use a grant agreement form that it has customized to apply to its particular program, as long as the grant agreement implements the provisions imposed by Minn. Stat. Sec. 16A.695. MMB strongly recommends that the Attorney General's office review each new customized grant agreement form to ensure that it properly reflects applicable requirements and statutory provisions.

3) Capital Appropriations with Non-State Matching Requirements

Minn. Stat. Sec. 16B.31, subd. 2, requires state capital improvement projects to have full funding. This statute specifies that *“No plan [for specifications for constructing or improving a state building or structure] may be adopted, and no improvement made or building constructed by the commissioner or any other agency to whom an appropriation is made for a capital improvement, that contemplates the expenditure for its completion of more money than the appropriation for it, unless otherwise provided in this section or the act making the appropriation.”*

Agencies and local government grantees must also follow Minn. Stat. Sec. 16A.502, which states, in part, *“If a state appropriation or grant for a capital project or project phase is not sufficient, by itself, to complete the project or project phase, and thus requires a commitment from other sources: (1) the commitment, including any required match, must be in an amount that, when added to the appropriation or grant, is sufficient to complete the project or project phase; and (2) the appropriation or grant is not available until the commissioner has determined that the commitment is sufficient.”*

Local projects are commonly required to provide non-state matching funds as a condition of receiving a state capital appropriation. Non-state funding may include federal, local and private funds.

The granting agency must provide sufficient documentation to MMB to verify that the recipient has complied with all matching requirements. This documentation must certify that non-state matching funds have been received, or the recipient has in place a legally binding commitment to secure the funding. Agencies should contact Gay Cerney at gay.cerney@state.mn.us, (651) 201-8049 for specific information on documentation requirements. Agencies must include appropriate documentation when they submit the Appropriation Entry (AP) form requesting that MMB activate the appropriation for the project. Once MMB approves the match, the appropriation will be activated.

If the project is intended to be completed in phases, the grantee must demonstrate that *all financing* is in place to complete the project or phase of the project that is envisioned in the appropriation language and as specified in the grant agreement. This additional information demonstrating full project funding is required when the Appropriation Entry form to activate the appropriation is submitted to the Executive Budget Officer at MMB.

For further information, please refer to MAPS operating policy 0302-02. Questions on matching requirements should be forwarded to your Executive Budget Officer.

4) Reimbursing Agencies or Local Governments

Agencies and local governments that receive a grant or a loan made from state general obligation bond proceeds often want to be reimbursed for past expenses which they have already paid from other funds. As a general rule, expenses that an agency or grantee pays from its own funds prior to the effective date of the bonding bill are not eligible to be reimbursed from bond proceeds.

The 2010 bonding bill (Laws 2010, chapter 189) became effective on March 15, 2010.

Federal tax law regulates the issuance and the use of tax-exempt bonds by states and local governments. The tax regulations severely limit the ability to use the proceeds of tax-exempt bonds to reimburse costs that have already been paid from other funds.

Agencies receiving reimbursement requests should not make any payments out of bond proceeds for project costs accrued prior to enactment of the bonding bill without first consulting MMB. Please contact Kathy Kardell at MMB (Kathy.Kardell@state.mn.us, (651) 201-8030) to discuss a grantee's particular circumstances.

5) Operating Program Review of Grantees for Bond-Financed Facilities

Agencies administering capital grant programs funded by bond proceeds have an expanded oversight responsibility to review the financial capability of a grant recipient's operating program.

Minn. Stat. Sec. 16A.695, subd. 5, requires that "*Recipients of grants from money appropriated from the bond proceeds fund must demonstrate to the commissioner of the agency making the grant that the recipient has the ability and a plan to fund the program intended for the facility.*"

MAPS operating policy 0302-04 suggests the type of financial review that agencies should conduct to satisfy this legal requirement. Certain types of financial information will need to be requested from grantees in the course of an agency's review process. Agencies that administer capital grant programs may wish to request that certain financial documents be included in the application materials submitted by grantees.

After completing a project's operating program funding review, agencies must provide a certification of the results of their program funding review to MMB.

6) Change in Fund Accounting for some Capital Projects

New GASB Statement No. 54 requires changes in fund accounting for certain capital appropriations starting with the 2010 bonding bill. Capital appropriations to be used to acquire, construct or improve property that will be owned by a state agency (including MnSCU, University of Minnesota and the Metropolitan Council) will be entered into the same fund as before. However, a new fund will need to be created for any 2010 capital appropriation that will be used to acquire, construct or improve property owned by a local government unit. Such projects that would previously have been entered in Fund 500, for example, should now be entered in new Fund 506. If agencies believe they received a capital appropriation involving grants to local governments that previously would have been entered into a fund other than Fund 500, please contact Gay Cerney at gay.cerney@state.mn.us or (651) 201-8049.

7) Qualified Capital Expenditures

General obligation bond proceeds may only be used for qualified capital expenditures. Eligible costs include land acquisition, predesign, design, construction, major remodeling (if it adds to the value or life of a building and is not of a recurring nature), and other improvements or acquisitions of tangible fixed assets of a capital nature.

General operating expenses, overhead, master planning, maintenance, operating costs, software and personal property such as computers are not qualified expenses. Equipment may be eligible if purchased and installed upon initial acquisition and construction of a building, expansion or major remodeling. Expenses that are not qualified capital expenses must be paid from funds other than general obligation bond proceeds or from general fund cash if not prohibited by law.

Agencies and grantees may use bond proceeds only for direct capital costs and not for depreciation, amortization, overhead, general administration or similar costs.

8) Staff Costs for Project Management

State agencies are strongly encouraged to charge the time of state employees working on capital projects to non-bond funding sources because of the undesirable practice of amortizing such salary costs over the 20-year life of state general obligation bonds. On October 20, 2009, MMB adopted a policy regarding use of general obligation bond proceeds to fund staff costs (<http://www.mmb.state.mn.us/doc/bonds/policy/bond-proceeds-fund-staff%20costs.pdf>).

Agencies may use general obligation bond proceeds to pay for staff costs effective with bonding appropriations authorized in the 2010 legislative session and for earlier appropriations if explicit statutory authority was given to use G.O. bond proceeds to fund staff costs.

Agencies must notify MMB of their intention to capitalize the costs of staff prior to expending any bond appropriations for this purpose. Staff time expended on capital projects must be tracked on a daily basis by project and by each individual recording time on the project. Agencies are required to submit a memorandum to their Executive Budget Officer, for approval by MMB, which outlines their proposed plans for tracking and reporting all agency staff time funded with G.O. bond proceeds and an estimate of total staff time to be charged to each project.

After approval of its plan by MMB, each agency must submit a quarterly report to its Executive Budget Officer detailing the staff costs being charged to each capital project. MMB will make a standard summary cover sheet available to agencies for submission of these reports. Following new legislation enacted in the 2010 bonding bill, MMB must now report annually to the legislature as to each agency's expenditures of capital appropriations for staff costs and its compliance with MMB's policy on staff costs.

9) Sustainable Building Guidelines for New Buildings; Alternative Energy Sources; Recycling Construction and Demolition Waste

All new state buildings funded after January 1, 2004 and all major renovations funded after January 1, 2009 from general obligation bond proceeds must follow the sustainable building guidelines and exceed the state energy code by thirty percent.

As required by state law, the Departments of Administration and Commerce have developed sustainable building design guidelines for all new state buildings. The primary objectives of these guidelines, known as the “B3 Guidelines”, concern the energy efficiency of new state buildings. Minn. Stat. Sec. 16B.325 specifies that these guidelines “... *are mandatory for all new buildings receiving funding from the bond proceeds fund after January 1, 2004, and for all major renovations receiving funding from the bond proceeds fund after January 1, 2009.*”

The Minnesota Sustainable Building Guidelines (MSBG) are available online at <http://www.msbg.umn.edu/> Questions regarding the MSBG should be directed to Garrett Mosiman at 612-625-8409, msbghelp@umn.edu.

For construction of a new building or renovation of at least half of an existing building, Minn. Stat. Sec. 16B.32 requires the commissioner of administration to include designs that utilize active and passive solar energy systems, earth sheltered construction, and other alternative energy sources where feasible.

New Minn. Stat. Sec. 16B.327 requires recycling of at least 50% of nonhazardous construction and demolition waste (measured by tonnage or volume) generated by construction, renovation or demolition of any building owned or leased by a state agency, MnSCU or the University of Minnesota. It applies to appropriations of \$5,000,000 or more enacted after January 1, 2011 (and thus does not apply to projects in the 2010 bonding bill) if a recycling facility is located within 40 miles of the project.

10) Predesign Review by the Department of Administration

As part of the state’s efforts to make better informed capital investment decisions, most agencies and grantees are required to prepare predesign documents for review by the Department of Administration before proceeding with design work (Minn. Stat. Sec. 16B.335, subd. 3).

The *Predesign Manual for Capital Budget Projects (Fifth Ed., Feb. 2010)* is posted on Administration’s Construction Services website, and can be accessed through the following link: <http://www.admin.state.mn.us/recs/cs/predesign/5thedition/Predesign%20Manual%20-5th%20Ed%20FINAL%20Feb2010.pdf>. Questions regarding the predesign process should be directed to Gordon Christofferson at Construction Services, gordon.christofferson@state.mn.us, (651) 201-2380.

11) Design Review by Legislative Committee Chairs

Paragraph (a) of Minn. Stat. Sec. 16B.335, subd. 1, restricts a recipient of a capital appropriation

from preparing “...*final plans and specifications for any construction, major remodeling, or land acquisition in anticipation of which the appropriation was made until the agency that will use the project has presented the program plan and cost estimates for all elements necessary to complete the project to the chair of the senate Finance Committee and the chair of the house of representatives Ways and Means Committee and the chairs have made their recommendations, and the chair of the house of representatives Capital Investment Committee is notified.*”

Paragraph (b) of this same statute exempts certain types of projects from the legislative design review requirements. This paragraph was amended in the 2010 bonding bill to exempt certain parking and transit facilities from the legislative design review requirements (see Laws 2010, ch. 189, sec. 34).

Please review this statute in its entirety and consult with the legislative chairs named in the statute for further information regarding the documents that must be submitted to meet applicable legislative design review requirements.

12) Up to One Percent for Art

Minn. Stat. Sec. 16B.35 allows an appropriation “*for the construction or alteration of any state building*” to include up to one percent for the acquisition of works of art for the public spaces of the building or its grounds. Please note section 7 of this memorandum regarding qualified capital expenditures. The “1% for Art” provision defines a state building as one where the construction or alteration is paid for, wholly or in part, by the state.

The law provides for three exemptions from the “1% for Art” provision: 1) building projects in state prisons; 2) projects where the state funding is less than \$500,000; and 3) projects where the Commissioner of Administration has determined that the provision is inappropriate.²

13) Project Cancellations

Minn. Stat. Sec. 16A.642 requires the Commissioner of MMB to report to the Legislature by January 1 of each odd-numbered year regarding unencumbered or unspent balances of capital appropriations enacted more than four years prior to that date. The reported amounts automatically cancel unless re-authorized by the Legislature.

The Commissioner will report the status of projects authorized in the 2010 bonding bill to the Legislature on January 1, 2015. All funding from the 2010 bonding bill that has not been contractually obligated or expended by that date will be cancelled effective the following July 1 unless it is re-appropriated by the Legislature. To avoid having a project included in the 2015 cancellation report, agencies and grantees should be prepared to move the project along to completion.

Questions regarding project cancellations may be directed to your assigned Executive Budget

² An example of a project where the “1% For Art” provision was determined to be inappropriate was a 2006 project to build a Biosafety Level 3 laboratory in the Agriculture and Health Joint Laboratory facility.

Officer or to Sue Gurrola, Treasury and Debt Management (Sue.Gurrola@state.mn.us or (651) 201-8046).

Additional Questions

Agencies should direct any additional questions to their assigned Executive Budget Officer at MMB or Gay Cerney, gay.cerney@state.mn.us, (651) 201-8049.