

NAHEFFA

National Association of Health & Educational Facilities Finance Authorities

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PRESIDENT'S MESSAGE

By Blaine Bandi

Last quarter, I welcomed you to the inaugural edition of the NAHEFFA newsletter. This quarter I am pleased to welcome you to the inaugural electronic edition of the NAHEFFA newsletter. NAHEFFA is pleased to provide this more environmentally friendly means of producing and distributing our newsletter. Electronic production and distribution also allows us to reduce distribution costs, shorten publication lead time, and facilitate broader distribution to interested parties. In the months to come, we will unveil our new logo and website. As a result, I will have at least one more inaugural opening to my President's Message before I have to think of something creative. The work of the Communications Committee in all these tasks is greatly appreciated.

Interesting Fact I:

It is impossible to lick your own elbow.

As we approach the summer months and prepare for vacations, baseball, swimming and other forms of recreation, it seems appropriate to reflect on the activities of the last few months. The sub prime mortgage crisis and rating agency downgrades of many of the bond insurers rippled through our industry and significantly disrupted the market for auction rate securities. Within months, many health and education borrowers experienced a doubling or tripling of their cost of debt. NAHEFFA responded quickly to organize a February conference call open to the membership. During the call, we learned the genesis of the auction rate crisis, the impact on

individual member Authorities, and shared ideas for facilitating borrower responses. More than 40 participants representing 30 Authorities joined the conference call. Subsequently, an additional 10 Authorities listened to a playback of the call. As we continue to assist our borrowers as they address their auction rate bonds, I want to thank all who participated in the call and subsequently shared ideas for addressing this crisis.

"Timing is everything" became the unofficial motto of our Spring Conference in DC. As most of you know, we typically schedule conference locations 2 – 3 years in advance. Our decision nearly 2 years ago to hold the 2008 Spring Conference in DC proved opportune if not prescient. Nearly 70 Authority representatives and guests attended the March 31 – April 2 conference. The auction rate crisis, overall concerns about the bond market and the economy, an energized and concerned membership, a reasoned and well defined NAHEFFA legislative agenda, and proximity to regulators, borrower advocates, and Congress all provided a perfect nexus for our Spring Conference. Attendees received timely updates and interacted with representatives of the Securities & Exchange Commission (SEC), Department of the Treasury, IRS, Municipal Securities Rulemaking Board (MSRB), Government Finance Officers Association (GFOA), Securities Industry and Financial Markets Association (SIFMA), American Hospital Association (AHA), National Rural Health Association (NRHA), Public Financial Management (PFM) and Ponder.

While in DC, we were honored to present Representative Phil English (R-PA) with the NAHEFFA Legislator of the Year Award in recognition of his dedicated service to non-profit healthcare and higher education. I extend my sincere thanks to William Bostic for an exceptional presentation and to Rep. English for his gracious acceptance, supportive words and generosity of time.

Within one week of the end of our conference, the House Ways and Means Committee adopted the FHLB Letter of Credit Provision. Thanks to the Federal Home Loan Bank (FHLB), state and local government supporters, and all of your efforts, we are an important step closer to passing this important legislation.

Interesting Fact II:

On average, 90% of you have already unsuccessfully attempted to disprove Interesting Fact I.

Have a safe and happy summer.

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FALL CONFERENCE ANNOUNCEMENT

The annual conference of NAHEFFA will take place September 24-26, 2008 in Seattle, Washington. Please watch your mail for registration information in the next couple of months. You will also be able to obtain forms and information on the NAHEFFA website (naheffa.com) in the near future. This site is currently under construction and forms/information will be available at www.naheffa.com or www.nchffa.com if the new site is not up and running when conference information is released. If you are interested in being a Sponsor, please watch the website, or contact Larry Nines, Executive Director of the Wisconsin Health and Educational Facilities Authority at (262) 792-0466.

WASHINGTON ADVOCACY REPORT

*By Charles A. Samuels and
Patrick D. Mara
Mintz Levin/ML Strategies
May 12, 2008*

1. FHLB Letter of Credit Legislation Passes House, H. R. 3221

As part of the housing and mortgage relief legislation, the NAHEFFA-backed Federal Home Loan Bank (FHLB) letter of credit legislation passed the House of Representatives in May. The legislation adds to the list of exemptions from the existing Internal Revenue Code "Federal Guarantee" prohibitions FHLB guarantees of bank letters of credit. As presently drafted, the new opportunity would apply for two years after enactment.

Originally, this legislation was aimed at assisting small institutions without credit ratings that otherwise would have difficulty entering the bond market or not be able to obtain reasonably priced financing. Recently, as the bond insurance crisis has affected even larger institutions, there is the possibility that these transactions could be used in larger offerings.

When the Treasury Department issued its Administration Statement of Position on the House legislation, it came out strongly against this provision. It is unknown, at this time, the significance of the Administration opposition to our provision. There is support in the Senate led by Senator Rockefeller of West Virginia and Senator Crapo of Idaho. Many NAHEFFA members have obtained co-sponsorship from their own senators. The House-Senate conference will likely soon work out the final resolution of the LOC legislation.

2. Renewed Interest in Bank Deductibility Legislation

Both Treasury and Congressional sources have indicated some interest in the liberalization of the bank deductibility rules which now strictly limit the incentive for banks to purchase tax-exempt bonds. In part, this is driven by the bond insurers attempting to find an alternative to the FHLB LOC legislation which they consider to be competitive. There is some possibility, however, that we may have an opportunity not only to liberalize the existing exemption for issuers (\$10 million) to something like \$30 million but also to allow the exemption for conduit issuers to be applied at the borrower level.

NAHEFFA members should emphasize both FHLB LOC's and bank deductibility in their Senate contacts.

3. 501(c)(3) Issuers Receive IRS Arbitrage Rebate Informational Audits/Surveys

A number of NAHEFFA members have received a request for information on arbitrage rebate as part of a continuing IRS campaign to investigate compliance tax requirements in 501(c)(3) financings. This program was announced by the IRS at NAHEFFA's Washington meeting.

4. Credit Rating Controversy Continues

Led by California State Treasurer, Lockyer, and supported by House Financial Services Committee Chair, Barney Frank, many governmental issuers are pursuing a campaign for changes in credit ratings for tax-exempt bonds so they are similar to corporate ratings. Some of the credit rating agencies are responding by creating a new "global" rating scale that would, to some extent, integrate muni ratings with corporate ratings.

See <http://www.treasurer.ca.gov/fairbondratings/>

In the non-profit financing sector, there has been less demand for these revisions.

5. The SEC expected to Approve EMMA in May

The Securities & Exchange Commission (SEC) is expected to propose changes to Rule 15C 2-12 so that the Municipal Securities Rulemaking Board (MSRB) can launch its municipal securities market web-based disclosure portal. This portal, which was described by MSRB Executive Director, Lynnette Hotchkiss, at the NAHEFFA Washington meeting, is called EMMA – Electronic Municipal Market Access. It is an internet-based disclosure portal which provides free public access to disclosure documents and real-time municipal security trade price data. EMMA has several stages through the end of 2008. The pilot phase provides official statements for new issues of municipal securities and related documents for advance refundings along with real time municipal securities trade price data. By the end of the year, there will be the full service phase subject to applicable SEC rules which will provide for submission in real-time and dissemination of all required continuing disclosures by issuers and obligated persons.

6. Bush Signs Student Loan Act into Law

In May, President Bush signed the Ensuring Continued Access to Student Loans Act of 2008, H.R. 5715, into law. The bill purports to ensure new protections so that students and parents are still able to have uninterrupted access to federal college loans even in tumultuous credit markets for federally guaranteed student loans. The law increases loan limits on federal unsubsidized student loans; allows payment deferral of federal PLUS college loans; and provides more authority to the Department of Education (DOE) to advance federal funds to guaranty agencies operating as lenders of last resort. DOE also could purchase loans from lenders in the federal guaranteed loan program.

WASHINGTON ADVOCACY REPORT

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7. Ways and Means Holds Hearing on Higher Education Incentives

The House Ways and Means Subcommittee on Select Revenue Measures held a hearing in early May on higher education tax incentives. In his opening statement, Subcommittee Chairman Richard Neal (D-MA) cited the increasingly rising costs of a college education. Neal, who has three children attending college, “took out a second mortgage” on his house, “got a second job teaching at UMass,” and borrowed from his retirement account, to fund higher education for his family members. During the hearing, the Government Accountability Office (GAO) witness stated that a full quarter of American taxpayers with education expenses do not claim the appropriate expenses or completely miss them. Half of those returns were prepared by tax professionals. In addition, most of the existing incentives merely bolster the affordability of higher education for students who are already in school. According to Neal, the incentives do not necessarily “help those for whom college is out of reach.”

At the same time, federal and state legislators continue to support mandatory payouts of large college endowments to provide greater access to low and middle income students. An amendment was proposed and withdrawn in a House higher education membership and is under discussion in Massachusetts.

8. House Passes Protecting Medicaid Safety Net Act of 2008

In late April, by a vote of 349 to 62, the House approved H.R. 5613, the Protecting the Medicaid Safety Net Act of 2008. The measure places a temporary one-year moratorium on seven Medicaid regulations. Without such a moratorium, the regulations would cause severe cuts to the Medicaid program over the next five years. Previously, the measure passed out of the Energy and Commerce Committee by a vote of 46-0. According to Energy and Commerce Committee Chairman John Dingell (D-MI), “H.R. 5613 will postpone the implementation

of these seven rules for one year, giving Congress time to evaluate the effect they could have on states, providers, and beneficiaries.” The bill is supported by all 50 state governors, many state legislators, state Medicaid directors, the National Association of Counties and over 2,000 national and local interest groups. H.R. 5613 will soon be considered by the Senate.

9. GAO Report Finds Health Savings Accounts Not Used By “Working Americans”

A recent GAO report detailed findings that the wealthy primarily use Health Savings Accounts (HSAs) as tax shelters. Ways and Means Health Subcommittee Chairman Pete Stark (D-CA) said of the study, “The GAO confirms that HSAs are not the way to meet the health care needs of most Americans.” In fact, one HSA company indicated some HSA funds were spent on casinos, bowling, and escort services, among other non-health related areas. There is legislation in the House, H.R. 5719, the Taxpayer Assistance and Simplification Act of 2008, requiring HSA holders to prove withdrawals are spent on qualifying medical expenses. HSAs grew from 438,000 to 4.5 million between 2004 and 2007.

10. Small Business Health Plan Bill Introduced in the Senate

Senate Health, Education, Labor and Pensions (HELP) Committee Ranking Member Mike Enzi (R-WY) introduced the bipartisan Small Business Health Plans Act of 2008 in April. The measure would allow working families and small businesses to pool together to purchase more affordable health insurance plans. As Enzi noted, “Small business health plans are one step toward making sure that every American has access to affordable health coverage.” The legislation allows associations to join together across state lines to provide their members with more affordable health coverage. This creates significant purchasing power that a small business would not have on its own. Enzi said he will continue to work with his Senate colleagues to “reach an agreement on small business health plans.” Original cosponsors of the bill include Senators Ben Nelson (D-NE) and Judd Gregg (R-NH).

A NEW VISION FOR ACCOUNTING

Get ready for possible big changes in accounting format from FASB, including reconfiguring the balance sheet and income statement to follow three categories of the cash-flow statement, requiring companies to report cash flows with the little-used direct method; and introducing a new reconciliation schedule that would highlight fair-value changes. Companies will also likely have to report more about their segments, possibly down to the same level of detail as they currently report for the consolidated statements. Meanwhile, net income is slated to disappear completely from GAAP financial statements, with no obvious replacement for such commonly used metrics as earnings per share. FASB, working with the International Accounting Standards Board (IASB) and accounting standards board in the United Kingdom and Japan, continues to work out the precise details of the new financial statements. CFOs and controllers at every publicly traded company in the world could be following these new changes as soon as 2010.

Net Income/Loss

From the outset, corporate financial officers have been ambivalent about FASB’s seven-year-old project, which was originally launched to address concerns that net income was losing relevance amid a proliferation of pro forma numbers. Critics point out that FASB will have little control over pro forma reporting no matter what it does. The FASB claims the project is not merely about getting rid of net income, but rather about capturing all income-related information in a single line (including such volatile items as gains and losses on cash-flow hedges, available-for-sale securities, and foreign-exchange translations) rather than footnoting them in other comprehensive income (OCI) as they are now.

Although finance chiefs are rallying behind net income, it is not clear that investors and analysts are excited about the prospect of losing net income, either. The official board pronouncement is that companies would still be allowed to segregate OCI items in the short term, but that they must appear on the main

A NEW VISION FOR ACCOUNTING

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income statement. Over the long term, the board plans a separate project to evaluate each OCI item and reconsider its placement.

Going Direct

Another major shift in the new model would be to require companies to use the direct method for the cash-flow statement, explaining cash changes from the bottom up to arrive at net income, rather than starting with net income and making adjustments. That statement would be linked with a new form, the so-called reconciliation schedule that would track changes in income to cash flows or fair-value changes. The difficulty in constructing a direct

cash-flow statement largely depends on the company. About 40% said constructing a direct cash flow statement would require major adjustments, while it would take minor adjustments for nearly 30%. The IASB, for one, doesn't think that the direct method should be required, and FASB members say they are looking closely at a hybrid direct/indirect method now used in Australia and New Zealand as a compromise.

Reconciliation Schedule

The concept of the reconciliation schedule, on the other hand, is gaining much wider support from Wall Street to some finance executives. The schedule should help a business understand the ability to generate recurring, persistent cash flows; and as more fair value comes through the financial statements, the

reconciliation schedule will do a better job of showing where those changes are coming from.

Finance executives so far are fairly relaxed about this proposal, largely due to Financial Accounting Standard 131, which says that they don't have to report externally anything that is not used internally. Given that FASB has so many big-picture projects on its plate these days, it is tempting to dismiss the financial-statement project as just another pie-in-the-sky idea that will get bogged down in procedure. But with a joint FASB/IASB draft due out for comment in mid-2008, decisions could be made by 2009, with implementation to follow by 2010 at the earliest, if not several years after that. *(Source: CFO; February 2008)*

BRIEFLY NOTED

... "Our ancestors may have come to America on different ships, but we are all in the same boat now". *(Source: Pastor Walter Harvey, Assembly of God Church)*

... Nationwide the amount employees paid for family health insurance coverage increased 30% from 2001 to 2005. The average cost in 2005 was \$10,728, with \$2,585 paid by the employee and \$8,143 paid by the employer. *(Source: Robert Wood Johnson; 04/30/08)*

... Rather than lending major works of art to existing public museums, more and more major art collectors are building their own museums to display their collections – thus limiting wide geographic access to major portions of their collections. *(Source: The Wall Street Journal; 04/04/08)*

... Many U.S. companies hoping to profit from surging exports created by the weak dollar are facing an unexpected hurdle: There aren't enough of the big, metal shipping containers that form the backbone of the shipping industry. *(Source: The Wall Street Journal; 04/10/08)*

... In 2004, almost 1/4 of all adult stays in U.S. community hospitals involved behavioral health including depression, bipolar, schizophrenia or substance abuse. *(Source: H&HN; April 2008)*

... Newspaper readership continues to decline at an accelerating pace, a sign that the migration of readers to online may be picking up speed. Average readership of 534 daily newspapers fell 3.6% for the six months ending 03/31/08. *(Source: The Wall Street Journal; 04/29/08)*

... The IRS released results of a post-issuance compliance check of 501(c)(3) organizations that used tax-exempt financing, finding that while 98% of responders said they had written procedures in place to ensure compliance, only 15% could verify that they actually implemented those written procedures. *(Source: Perkins Coie LLP; 04/24/08)*

... As the number of specialist physicians and family practice doctors has grown, the number of general surgeons has dropped from 14.7 per 100,000 people in 1980 to 12.8 in 2005. *(Source: H&HN; March 2008)*

... A recent survey of physicians shows 59% support a national health insurance plan involving a single federally administered social insurance fund that guarantees health coverage for everyone. *(Source: Washington Post; 03/31/08)*

... Tax free money market funds surpassed \$500 billion for the first time April 7th. By comparison, taxable money market funds stood at \$2.985 trillion. *(Source: The Bond Buyer; 04/11/08)*

... U.S. hospitals employed more than 5 million people in 2006 and had an economic benefit of \$1.9 trillion. *(Source: American Hospital Association; 04/07/08)*

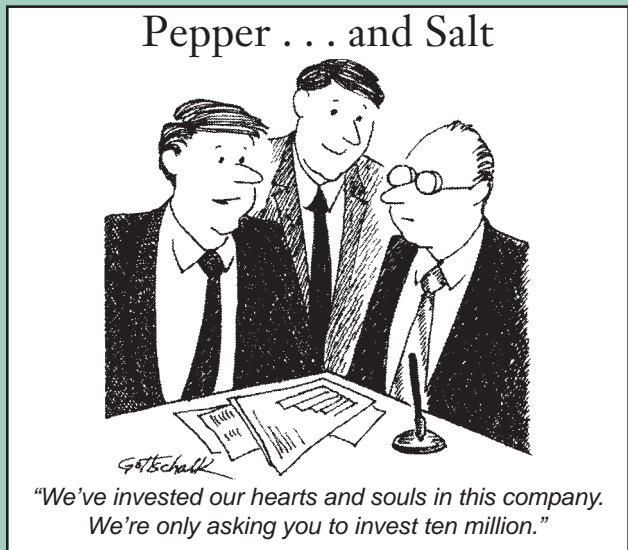
... Flat funding from the National Institutes of Health threatens a generation of younger researchers and breakthroughs in health care. In 1990, young researchers received 29% of NIH dollars. By 2007, that had dropped to 25%. *(Source: cseper blog; 03/11/08)*

... Backed by a strong economy and growing stock market, American colleges and universities raised an estimated \$29.8 billion from donors in 2007. *(Source: The Chronicle of Higher Education; 02/29/08)*

BRIEFLY NOTED

Continued from page 4

- ... Baseball commissioner Bud Selig was paid \$15.06 million for the fiscal year ending October 31, 2006. This represents a 4% increase from the previous fiscal year. *(Source: Milwaukee Journal Sentinel; 03/12/08)*
- ... 750 colleges and universities now offer some sort of test optional admission process. In place of test scores, applicants are admitted based on activities and class curriculum. *(Source: Milwaukee Journal Sentinel; 03/24/08)*
- ... For the first time in history (2008), more than half of the world's populations (about 3.3 billion people) are living in urban areas, this according to the United Nations Population fund. *(Source: USA Weekend; 02/08/08)*
- ... Because of technological advances, a new generation of larger, more powerful land based telescopes are about to be put into service. Costs for such instruments range from \$500 million to \$1.2 billion. *(Source: Associated Press; 02/10/08)*
- ... A new seed vault is now open deep beneath an Arctic mountain in Norway. Capable of holding up to 4.5 million seed samples, the vault is capable of withstanding earthquakes and nuclear attacks. There are 1,400 other less secure seed banks throughout the world to protect the world's plant populations from global catastrophe. *(Source: TIME; 02/11/08)*
- ... More corporations are designing and paying for high school classes which direct students to develop interests and skills in their industry. Participants include accounting, manufacturing/engineering and IT entities. *(Source: The Wall Street Journal; 03/06/08)*
- ... There are currently 82 million cats in America and 72 million dogs. The total pet population is now over 282 million with 60% of all homes having at least one pet and 21% having five or more. *(Source: USA Weekend; 01/25/08)*
- ... Worldwide golf ball production now exceeds 1.2 billion balls each year. Where do all these golf balls go? *(Source: The Wall Street Journal; 01/26/08)*
- ... About one in every five health care dollars in the U.S. is spent caring for persons with diabetes. *(Source: Washington Post; 01/25/08)*
- ... The American Red Cross is cutting a third of the 3,000 jobs at its national headquarters in an effort intended to eliminate a \$200 million deficit within two years. *(Source: Associated Press; 04/15/08)*
- ... The demand for elderly adult day care is growing between 5% and 15% each year in place of nursing home placements. Such programs can provide a stimulating social environment at substantially less cost. *(Source: McKnights Online; 01/11/08)*
- ... Teaching vacancies in K-12 public schools are filled with substitute teachers 30% of the time. The average student in their career from kindergarten through high school can expect to have substitute teachers for the equivalent of one full school year. *(Source: Associated Press; 01/17/08)*
- ... The average wait time in a hospital emergency room was 30 minutes in 2004, up from 22 minutes in 1997. *(Source: Washington Post; 01/15/08)*
- ... 76 colleges and universities now have endowments in excess of \$1 billion. Sixteen joined this list in 2007. *(Source: Associated Press; 01/24/08)*
- ... Economic slowdowns and job declines have historically resulted in increased enrollment in higher education, particularly 2 year technical and community colleges. *(Source: The Chronicle of Higher Education; 02/08/08)*
- ... About 1/4 of the 47 million Americans who don't have health insurance are eligible for Medicaid and State Children's Health Insurance Programs, but they aren't enrolled. *(Source: Washington Post; 04/25/08)*
- ... As our oceans are absorbing more carbon dioxide and other greenhouse gases, they are becoming more acidic, risking the oceanic food chain. *(Source: McClatchy News Service; 12/23/07)*
- ... With 4.3 million births in 2006, the United States is experiencing a baby boomlet of the highest birthrates since 1961. Reasons given include: a drop in contraceptive use; drop in access to abortion; poor education and poverty. Culturally, Hispanic Americans have fertility rates 40% higher than the U.S. average. *(Source: Associated Press; 01/16/08)*



Source: The Wall Street Journal

TURMOIL IN THE STUDENT LOAN INDUSTRY

Several student-loan lenders are backing out of the federal program, the result of the credit crunch and government subsidy cuts that have made the business of lending to students increasingly unprofitable. Big banks such as Citigroup Inc. and Wells Fargo & Co., might be reluctant to pick up the slack as other lenders exit, because they are already stretched by the credit crisis. The government, already a big student lender, could step in to shore up the system, although that would be complicated.

Brazos Higher Education Service Corp. is one of the latest lenders to suspend new loans to students through the Federal Family Education Loans program, or FFEL, for the 2008-2009 academic year. Brazos, a 33-year-old company based in Waco, Texas, is one of the nation's largest student lenders, with a portfolio of \$15 billion in education loans. It joins a list of at least 26 other lenders that have stopped providing such loans, according to FinAid.org, a student-financial-aid publication.

An estimated eight million students and parents will seek \$109 billion through FFEL for the coming fiscal year, according to Education Department data. If lending continues to tighten, it could push up their costs. Education Department officials maintain that with nearly 2,000 lenders taking part in the FFEL program, others, particularly banks, will pick up the volume from institutions that stop lending.

As institutions like Brazos continue to suspend their student loan programs, schools like Augustana College in Rock Island, Illinois, are starting to take another look at the federal government's direct student-loan program. This fall, Augustana will stop doing business with FFEL lenders and join the federal direct-lending program. Under it, students borrow from the federal government through their colleges, and private lenders are eliminated from the picture.

So far this year, nearly 60 other institutions have moved to direct lending or applied to do so- including Pennsylvania State University,

Boston's Northeastern University, Ohio's Mount Vernon Nazarene University; and Northern Illinois University.

Private lenders still dominate the federal student-loan market, estimated at \$114.8 billion in fiscal 2007 and about 4,500 colleges and other institutions actively take part in the FFEL program, compared with just over a thousand for direct lending. But for the many students whose schools don't participate in direct lending, borrowing stands to be more expensive for the 2008-2009 academic year, as private-lender rebates disappear. *(Source: The Wall Street Journal; 03/25/08)*

2008 PREDICTIONS FOR TRENDS IN HEALTH CARE

As costs and the numbers of uninsured keep trending upward, health care has emerged as the most important domestic issue of 2008. Here are PricewaterhouseCooper's Health Research Institute's predictions for the top eight health industry issues of the coming year:

1. Hospital coffers will feel the impact of a new Medicare reimbursement system that's designed to better recognize the severity of patient illnesses. Specialty hospitals and others that see less acutely ill patients could see their revenues decline, while urban hospitals that treat sicker patients could benefit.
2. Increased oversight and authority by the U.S. Food and Drug Administration may boost the public's trust in drug safety, but also could add to the regulatory burdens on pharmaceutical companies. The FDA now may require drug companies to conduct additional clinical trials to assess risks associated with a drug after it has been released to the public.
3. A surge in the number of retail health clinics, such as those in drug stores, will force states, payers and policymakers to think about the best ways to deliver primary care. Hospitals could benefit from retail clinics if they draw uninsured patients, while pharmaceutical companies

may need to market more to the nurse practitioners who run the clinics.

4. The market for individual health insurance could get much broader if other states and the federal government follow the lead of Massachusetts, which requires that all residents have coverage. Individual coverage also could get a boost from Republican proposals for tax incentives to help consumers buy individual policies.
5. Retirees are playing a greater role in funding their health-care coverage, whether they like it or not. As the population ages and health-care costs increase, employers are shifting more responsibility for retiree coverage to the retirees. In a PricewaterhouseCoopers survey of multinational company executives, 73% said they needed to reduce contributions to retiree health coverage and cap benefits.
6. Big pharmaceutical companies, groaning under the high price of drug development, will keep buying and collaborating with life-science companies to stock their product pipelines. But biogenerics-generic copies of biological drugs- could crimp drug company revenues.
7. New IRS rules will mandate that nonprofit hospitals uniformly disclose more details about the community benefits they provide, such as charity care. To justify their tax-exempt status, hospitals also will have to be more forthcoming about executive salaries and benefits.
8. Asia is poised to become the world's largest pharmaceutical consumer and producer. American drug companies have increased their marketing and clinical trials in Asia because of the market's size, increasing wealth and growing awareness of health-related issues. On the production side, much of Asia provides high-quality, inexpensive labor. But watch out: Several Asian drug companies aim to become worldwide pharmaceutical powerhouses, not just contract manufacturers.

(Source: KansasCity.com; 01/14/08)

CONTROLLING CONSTRUCTION COSTS

*By Mark MacDonald,
Wipfli LLP*

Despite the bad news in the media about the economy, there is quite a bit of construction activity going on across the nation. The changing demographics are putting strains on existing medical office buildings, hospitals, long-term care facilities, and schools. The result is construction cranes are appearing on campuses and medical grounds for new buildings, additions and major renovations. Capital projects are complex and expensive activities. In fact, a major construction project may be among the largest financial transactions an organization ever makes. Construction projects expose the owner to major financial risks that are much different than those encountered in its day-to-day operations.

Many organizations lack the expertise, manpower, and time necessary to successfully manage a capital project and, in most cases, they cannot justify adding personnel just to manage construction projects.

Construction compliance services can ensure that a capital project is completed on time, to expectations, and within budget. With effective tools and industry experience, the right services help an owner successfully manage each of the three phases of construction.

Preconstruction

Developing sound financial controls should be done before jobsite activity begins. Good controls begin with the proper contract language. The reality is the contractor's definition of costs is usually quite a bit different than the owner's understanding of the term.

Owners are often quick to accept contract language without reviewing the definitions for reimbursable costs, change order pricing, non-reimbursable costs, and the procedures the owner and contractor must follow over the life of the project. The contract contains the

very controls that will either protect the owner from paying too much for construction work or subject the owner to unnecessary costs.

One hospital accepted contract language that allowed the contractor to charge for data-processing equipment based on supervisory hours, instead of actual costs. The hospital paid the contractor about \$150,000 more than they should have if the contract wording was adjusted.

During this phase, the owner should assemble the internal project team and assign project responsibilities to its members. With proper procedures and checklists in place before a project begins, an owner can better manage change orders, approve contractor payments, and ensure that actual construction is being completed according to plan.

Construction

A contractor must have adequate controls to accurately capture the financial activity of the project. An owner may not have the industry experience to determine that the contractor's controls exist and are effective.

A knowledgeable construction compliance team can help an owner avoid potential overcharges before they are paid by analyzing change orders, performing site visits, and reviewing invoices for errors and costs that do not comply with the contract terms.

One common area for savings is supervisory labor costs. Project managers, superintendents and engineers are normally salaried, yet contractors charge an hourly rate for their time. We have discovered some contractors charging owners for supervisory personnel when they were on vacation and holidays, even though the labor rates included a markup for vacation time.

Closeout

When the time for final payment arrives, there are often questions about change orders or for some reason the owner is uncomfortable with the final results of the project. At this time, many owners choose to engage a construction compliance services team to provide assurance that a fair price was paid for the construction work performed.

The services verify change orders are valid and priced correctly, confirm payments to subcontractors were proper, and verify the owner has received the "as-built" drawings, operating manuals, and final lien waivers before making the final payment and releasing retainage.

Trust...but verify

An owner may decide to use construction compliance services at any time during the project or at any stage of construction.

Organizations use construction compliance services to help manage capital projects and avoid unnecessary costs. Our clients have estimated that employing construction compliance services over the life of the project have resulted in savings of eight to ten dollars for every dollar paid for the services.

Owners that choose only a close-out audit after the completion of a construction project normally find overcharges of up to 2% of construction costs.

With the right controls and reviews in place, the services further ensure that all parties know what is expected of them, resulting in fewer conflicts during the construction period and less occurrences of litigation.

About the author:

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STATE HAPPENINGS

MINNESOTA

21st Annual Conference on Tax Exempt Financing

The Minnesota Higher Education Facilities Authority presented its 21st Annual Conference on Tax Exempt Financing on April 16, 2008. College business officers and finance industry professionals heard presentations on the new EMMA system, post-issuance compliance and recordkeeping, current financing market issues, national and state trends in higher education credit and emerging technology. Speakers included credit analysts from Moody's and Standard & Poor's.

WASHINGTON

Staff Changes

Claire Petersky, Manager of the Washington Higher Education Facilities Authority, resigned from her position effective May 1, 2008. A replacement to fill her position is being sought.

WISCONSIN

11th Annual Workshop a Success

On March 10, 2008, the Wisconsin Health & Educational Facilities Authority (WHEFA) hosted its 11th annual Insights Into Capital Finance Workshop. Topics included: Current Issues Affecting Capital Finance; a Washington DC Legislative Update; Successful Application of Lean Thinking in the Healthcare and Education Sectors; Creating and Maintaining an Effective Bond Issuance Compliance Program; and Effectively Incorporating "Green" Construction into the Healthcare and Education Sectors. All presentations are posted on the WHEFA website (whefa.com). Just click on the Workshop link to view presentations that may be of interest.

NAHEFFA

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