STATE OF NEBRASKA

MASTER LEASE PURCHASE PROGRAM

State Accounting

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Policy on the Master Lease Purchase Program (MLPP)

Overview of the Program

In conjunction with §81-1107, which requires the Administrative Services (AS) to review and approve financing agreements of the state, AS implemented in 1994 a Master Lease Purchase Program (MLPP) for the purpose of obtaining tax exempt lease financing.

There are many ways for agencies within the State of Nebraska to purchase fixed assets. Preferably, these purchases should be made with cash through annual budget appropriations. Occasionally, situations arise where agencies need to make significant, one-time purchases (such as data processing, telecommunications, laboratory, motor vehicle and other essential equipment) that their annual budget appropriations cannot accommodate. When such situations arise, agencies may inquire with State Accounting regarding the feasibility of a new Master Lease Issue. The MLPP is available to provide agencies a method to finance significant equipment acquisitions.

Financing agreements related to real property acquisitions and capital construction projects may be financed only with prior legislative appropriation. Please refer to §81-1107 (3) for more detail on financing these types of projects.

Once financing via the MLPP is determined to be feasible, and if Master Lease Financing is approved at the agency level and by the Administrative Services, State Accounting will work with the Trustee, Underwriter, and Bond Counsel on creation of a new Master Lease issue.

The MLPP is only a financing mechanism. All appropriate State purchase-approval procedures must be followed. The procedure on creating a fixed asset in NIS for equipment financed through the MLPP can be found on the NIS Training Manual: http://www.das.state.ne.us/nis/trainingmanuals/810_training_manuals/fa/004_FA_WI_L1_T1.b_Master_Lease_Info.pdf

The following information summarizes the MLPP:

Amounts to be Financed	Normally, equipment costing not less than $50,000 and not more than $5,000,000.00 (Amounts less than $50,000.00 may be considered on a case by case basis. Amounts less than $600,000.00 will only be considered if they are to be included with a larger issue).
Repayment Provisions	Agencies will pay for the financing through level monthly payments to State Accounting over life of the lease.
Repayment Terms	Will be negotiated for each equipment group with a term not to exceed the expected life of the equipment being leased. For most equipment this will normally be three (3) to five (5) years.

Parties to the Master Lease To finalize a Master Lease there are four parties to the transaction:

1. AS State Accounting represents the State and its agencies.
2. Bond Counsel prepares all legal documents.
3. The Underwriter markets and sells the instruments (Certificates of Participation) to the public from which the funds are obtained to provide to the agencies. The underwriter also acts as the lessor.
4. The Trustee (a bank) receives the proceeds from the sale of the certificates of participation and pays for the equipment purchased from such proceeds. The Trustee holds onto the funds until all equipment is purchased.

Interest Rate The rate will be set at the time the lease for the equipment is finalized, at which time the rate will not exceed 101% of the market rate of comparable "Aa3" rated, annual appropriation lease financings.

Fees and Expenses The underwriter will be paid a one-time fee (discount) of .675% for issues $3,000,000.00 and under, and .725% for issues that exceed $3,000,000.00. Other fees include legal fees (.15%), trustee fees ($1,500 at closing, and $1,500 annually), and printing fees (amounts vary). These fees will normally be part of the amount financed and paid over the term of the repayment period. A schedule of the total payments including principal, interest and fees will be provided to the borrowing agency at the inception of the lease.

Title to the Equipment Title will be held by the State of Nebraska, with the lessor being given a security interest in the equipment until the Master Lease commitment is paid in full.

Modification of Equipment: The State shall, at its own expense, have the right to make repairs, replacements, improvements, substitutions and modifications to the equipment. Such work shall then comprise part of the equipment and be subject to the provisions of the lease. Upon the completion of any such work, the value of the equipment shall not be less than that immediately prior to the commencement of such work.

Agency(s) Payments: The State represents that it intends to continue a lease for its entire lease term and to pay all rental payments relating thereto. The person or entity in charge of preparing each agency(s)'s budget will include in the budget request for each fiscal period the rental payments to become due in such fiscal period and use all reasonable and lawful means available to secure the appropriation of funds. Nonappropriation is defined as an act that specifically prohibits the State from performing its obligations under the MLPP.

In planning for utilizing the MLPP, agencies should plan on the process taking 6-8 weeks from the time we notify the underwriter that we want to use the MLPP until the issue is finalized and the agency(s) will have access to the proceeds.

Federal regulations allow agencies to master lease equipment that has been purchased prior to establishing a Master Lease. In order to include such purchases, agencies must complete a "Certificate of Official Intent". See "Step 3" on page 7 for process sequence.

The funding of projects through the MLPP is explained on pages 7-11; however, it is important that the agency(s) must spend all the proceeds plus any interest earned from unspent proceeds according to the following schedule:

Within 6 months - 15% of original funds financed plus interest
Within 12 months - 60% of original funds financed plus interest
Within 18 months - 100% of original funds financed plus interest

State Accounting will work with agency(s) when the project is almost complete to ensure all funds (including interest) are spent. If the above spending requirements are not met, agency(s) will be subject to significant arbitrage payments.

Arbitrage is defined as "The nearly simultaneous purchase of a good or asset in one market where the price is low, and sale of the same good or asset in another market where the price is higher". As it relates to the MLPP, Federal Regulations prohibit State Governments from borrowing funds at a low interest rate, and then earning a higher interest rate on this money prior to it being spent. For instance, if the rate of interest on the M/L issue is 4% and your unspent proceeds earned 5%, and you didn't spend the proceeds in accordance with the spending schedule, then you have incurred arbitrage which must be paid to the federal government.

Preparatory Procedures

Step 1

When a State agency(s) identify situations where they need to make significant, one-time equipment purchases that their annual budget appropriations cannot accommodate, the agency(s) should notify State Accounting of the possibility of needing Master Lease (M/L) financing.

**Requests that include real property acquisitions and/or capital construction projects must receive legislative appropriation prior to pursuing Master Lease financing. Please see §81-1107 for more detail on these types of requests.

Step 2

State Accounting can provide estimates of interest rates, repayment terms and tentative amortization schedules for equipment purchased through the MLPP. The agency(s) can then compare the M/L costs with other methods of financing, or decide to pay for the purchase with current cash/appropriations.

Step 3

If there is a possibility that the agency / division will finance this equipment, they should complete a "Certificate of Official Intent". This will allow agencies to retroactively include equipment that has been purchased as much as 60 days prior to the completion of such Certificate. Completing the "Certificate of Official Intent" then gives the agency an additional 18 months to finalize a new master lease issue. There is no need to complete this form if there is no possibility that the equipment will be purchased prior to the finalization of the lease documents. However, you cannot Master Lease equipment purchased prior to the closing date without this form being completed. Agencies will be require to provide State Accounting the amount of purchase prior to finalization of the lease documents.

Step 4

If the agency / division determines that it wants to finance through the MLPP, they should provide an official Master Lease Request to State Accounting. This should include the signed "Agency Authorization Form" and the "Equipment Schedule". State Accounting will pursue a new issue under the MLPP at such time when there are equipment purchase needs large enough to make a new Master Lease issue feasible.

Step 5

State Accounting will submit the formalized Master Lease request package to the applicable Budget Analyst to obtain Budget approval, ensuring the agency(s) does not have either the cash or the appropriations specifically identified to pay for the equipment in the current year.

Step 6

After Budget approval, State Accounting submits the entire M/L request package to AS Director to obtain approval on the pending M/L Issue.

Step 7

State Accounting notifies Bond Counsel, Underwriter, and Trustee to proceed on the new Master Lease Issue.

Step 8

Letter requesting Attorney General's opinion related to Master Lease offering is signed by AS Director and sent to AS Legal for review and forwarding to the Attorney General's office. AS Legal will inform Policy Research Office of such request. State Accounting will also obtain other documents for the new master lease issue closing transcripts.

Step 9

State Accounting works with the above parties in providing necessary information to finalize the lease. This includes identifying the structure of the new lease, setting accounts, the repayment period, and the timing of the principal and interest payments.

Master Lease Maintenance Process

1. Upon determination that a new issue under the Master Lease Purchase Program (MLPP) is needed, the State of Nebraska, represented by and acting through the Department of Administrative Services (AS), as lessee, enters into a Master Lease with Option to Purchase Agreement with a Bank Trustee, who acts for and on behalf of the underwriter, who is the lessor. AS is assisted in this process by outside Bond Counsel.

2. The Trustee secures funding as a result of the issuance and sale of Certificates of Participation (Certificates) to the public through the underwriter contracted by the State of Nebraska.

3. The Trustee deposits the funds received, less cost of issuance, into the Project Fund. Such funds are held by the Trustee on the agency(s) behalf.

4. State Accounting will forward a final amortization schedule to the agency(s) / division(s).

5. Unless the agency division has already properly purchased the equipment and previously signed a Certificate of Official Intent, then regular purchasing procedures should be followed to procure the equipment. After the equipment is accepted, Agencies must create an asset in the General Ledger by following procedures located in the NIS Training Manual.

6. Agency(s) will submit the approved invoice(s) to State Accounting. State Accounting will complete a cover letter, Form of Payment Request, and a Certificate of Acceptance and forward to Trustee.

7. Funds are disbursed by the Trustee from the Project Fund to pay vendors the purchase price of the Equipment. Interest will be earned on these funds until all funds are disbursed from the Project Fund. Such interest can be used by the agency / division to purchase equipment. Unspent interest will be used to pay down on the amount owed by the agency / division.

8. State Accounting initiates monthly payments from the agency / division users to the Master Lease Trust Fund via a journal entry. State Accounting retains any interest earned on such billings as mandated by State Statute (81-1108.03).

9. State Accounting makes the semi-annual payments to the Trustee from the Master Lease Repayment Fund so the Trustee can repay the certificate holders. These payments utilize the agency lease payments that have been made to State Accounting.

10. On behalf of the lesser, the Trustee makes principal and interest payments to the holders of the Certificates when due.

Questions & Answers

Q: When should I Master Lease?
A: Whenever your agency is making significant equipment and/or services purchases and wants to spread the costs of the purchase over several budget periods and your current cash/appropriations will not be able to pay for equipment in the current year.

Q: How do I pay a vendor for M/L purchased equipment and/or services?
A: All invoices for equipment or services that are purchased under the MLPP must be submitted to State Accounting. These requests are then processed, and forwarded to the Trustee, who pays the vendor directly out of the Master Lease Project Fund.

Q: How do MLPP monthly payments work?
A: State Accounting will directly withdraw predetermined amounts from the Master Leasing Agency by the 10^{th} of each month (via a journal entry). Such predetermined withdrawl amounts will be provided to agencies via an amortization schedule (see example on page 20). These agencies will direct State Accounting which business units to use when processing monthly billings.

Q: Are there any hidden costs to the MLPP?
A: If the funds are spent appropriately, and in a timely manner, there are no hidden costs. All costs, including principal, interest, and fees are disclosed to the agencies. However, if the funds are not spent timely, and according to federal regulations, arbitrage fees may be applicable.

Arbitrage is defined as "The nearly simultaneous purchase of a good or asset in one market where the price is low, and sale of the same good or asset in another market where the price is higher". Federal Regulations prohibit State Governments from benefiting from arbitrage activities.