

# SOUTH DAKOTA BOARD OF REGENTS

## Policy Manual

**SUBJECT:** Auxiliary Revenue System

**NUMBER:** 5:25

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### **A. PURPOSE**

To establish the necessary fund structure and the appropriate flow of funds generated by the Auxiliary System to capture the appropriate financial information necessary for continuing disclosure.

### **B. DEFINITIONS**

1. **Auxiliary System:** On October 21, 2004, the Board established a combined system of housing and auxiliary facilities for all six universities to leverage the strength of the system for bonding purposes, this is referred to as the Auxiliary System.
2. **Board:** The Board means the South Dakota Board of Regents.
3. **Bond or Bonds:** A series of housing and auxiliary facilities system revenue bonds.
4. **Bond and Interest Sinking Fund Account:** An account of that name established for each Institutional System pursuant to the requirements of each bond resolution.
5. **Capitalized Interest Subaccount:** A separate and special fund must be created with each bond issue at each Institution into which bond proceeds equal to the interest costs over a designated period shall be deposited.
6. **Construction Fund:** A separate and special fund created with each bond issue at each institution in which the proceeds of the bond issue applicable to construction of the project will be deposited.
7. **Debt Service Reserve Account:** A fund of that name established for each institutional system pursuant to the requirements of each bond resolution. A debt service reserve account is not required by all bond resolutions.
8. **Electronic Municipal Market Access (EMMA):** The Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Market Access system for municipal securities or any other electronic format or system prescribed by the MSRB.
9. **Gross Revenues:** All fees, rentals, and other charges from students, staff members, and others using or being served by any portion of the facilities comprising an institutional system.
10. **Institution:** Institution means Black Hills State University, Dakota State University, Northern State University, South Dakota State University, South Dakota School of Mines

and Technology, University of South Dakota, and any other institution which becomes part of the system.

- 11. Institutional System:** The existing facilities of each institution as described in Exhibit A of the most recent Bond Resolution.
- 12. Net Revenues:** The portion of gross revenues of an institution remaining after providing sufficient funds for the reasonable and necessary cost of currently maintaining, repairing, insuring, and operating the institutional system, including the related operating reserve.
- 13. Operating Reserve:** Such amount as is adequate and necessary for working capital for operation of the institutional system, provided such operating reserve shall not exceed one-fourth of the operating and maintenance expenses of such institutional system for the preceding 12 months.
- 14. Permitted Investments:** Any investments permitted by the laws of the State of South Dakota for the investment of public funds.
- 15. Pledge of Revenues:** All revenues generated by the Auxiliary system are deemed as pledged towards the payment of the bonds.
- 16. Project(s):** Facilities to be constructed with a series of bonds.
- 17. Repair and Replacement Reserve Account (RRR):** The account of that name for each institutional system established pursuant to the requirements of a bond resolution. Dollars required for RRR requirement are deposited in this account.
- 18. Revenue Fund:** The fund of that name established for each institutional system pursuant to the requirements of a bond resolution. An amount equal to 5% of the cost of construction, furnishing and equipping of all facilities in such institutional system.
- 19. Maximum Annual Debt Service:** The largest amount of debt service due in any single fiscal year over the life of the bond.

## **C. POLICY**

On October 21, 2004, the Board established a combined system of housing and auxiliary facilities for all six universities to leverage the strength of the system for bonding purposes, this is referred to as the Auxiliary System. Under this resolution and authority in South Dakota statute, the Board may issue bonds for the purposes of financing the construction, acquisition, or modification of revenue generating facilities. The Auxiliary System provides that each institution can continue to operate its existing auxiliaries with central oversight, but the revenues are subject to cross-collateralization to avoid a potential default on any bond issued on behalf of any institution. The bond covenants and required due diligence establish the requirements for the operation and longevity of the Auxiliary System. The flow of funds and the reporting of financial information are the focus of this policy.

### **1. Bond Proceeds Deposited into Either a Construction Fund or a Capitalized Interest Fund at the Campus Level**

#### **1.1. Construction Fund**

All monies held in the construction fund shall be used or held for use solely for the payment of the cost of construction for the project(s) approved by the Board. The monies in the construction fund that are not needed for expenditures may be invested and reinvested in permitted investments. Interest from such investments prior to completion of the project(s), if the proceeds from the sale of the bonds plus earned interest exceed the cost of the project(s), shall be:

- Paid into the Bond and Interest Sinking Fund and used for the payment of the next interest payment of the bond, or
- Used for any purpose approved by the Board and bond counsel.

#### 1.2. Capitalized Interest Fund

The Capitalized Fund is made up of bond proceeds to be used for the payment of interest on a bond for which the pledged revenue stream has not begun or is temporarily halted due to construction. The monies in the capitalized interest fund may be invested and reinvested in permitted investments. Interest from such investments prior to completion of the project(s) shall be deposited in the construction fund.

## 2. Flow of Funds from Pledged Revenues

### 2.1. Revenue Fund

The gross revenue of each institution will be credited to a special account for each institution known as the Housing and Auxiliary Facilities Revenue Fund. Each revenue fund shall be maintained as a special account, separate and apart from all other funds of the institution and shall be maintained by the institution so long as any bonds are outstanding. The monies in each revenue fund shall be used and expended first to maintain the institution's operating reserve. Funds shall be applied to pay when due all necessary operating expenses, which include current maintenance charges, expenses of reasonable upkeep and repairs, properly allocated share of charges for insurance, and all other expense incident to the operation of the institutional system, but shall exclude depreciation, all general administrative expenses of the institution not allocable to the institutional system, and the payments required to be made into the institution's RRR account.

### 2.2. Bond and Interest Sinking Fund Account and Debt Service Account

A separate account for each institution shall be established and maintained. On or before each March 25 and September 25 (or other date if provided by a specific series of bonds) after payment of operation and maintenance expenses of the institutional system due, the chief financial officer of the institution shall transfer to the Bond and Interest Sinking Fund account such amounts which, when added to the balance therein, will be sufficient to equal the interest then due on the bonds and one-half of the principal due within the next 12 months. The funds necessary to pay the principal and interest on the bonds due on the immediately following payment date shall be immediately transferred to a separate account, known as the Debt Service Account. All monies credited to the Debt Service Account are irrevocably pledged to and shall be used solely for the payment of principal and interest on the bonds of the institution.

### 2.3. Debt Service Reserve Account

Irrevocably pledged to and solely used as described by the bond resolution. Not all bond issues require a debt service reserve. If required, a separate subaccount is created for each series of bonds. The amount of funds to be deposited in the account is the lesser of the maximum annual debt service, 125% of the average annual debt service, or 10% of the original principal amount of the bonds. Funds on deposit in such a subaccount may be transferred to the related institution's debt service account and used to pay debt service on the bonds secured by such subaccount in the event funds on deposit are insufficient for bond and interest payment. In the event the amounts of deposits exceed the debt service reserve requirement, the excess may be withdrawn and used to pay debt service on the bonds they are securing. If on any April 1 or October 1, the amount on deposit in the debt service reserve account is less than the debt service reserve requirement, the Board shall transfer funds from the related institution's revenue fund and deposit into such subaccount no later than the next interest payment date on such bonds in an amount not less than that necessary to restore the subaccount to the debt service reserve requirement.

### 2.4. Repair and Replace Reserve

On or before the close of each fiscal year, a minimum of 10% of the amount transferred to each Institution's Bond and Interest Sinking Fund shall be transferred from each institution's revenue fund to the RRR account until an amount equal to the RRR requirement of each institution has been accumulated. Transfers need not be made at any time when funds and investments in the RRR account exceed the RRR requirement. All moneys and investments held in the RRR shall be used and held for use to pay the cost of unusual or extraordinary maintenance or repairs, renewals, renovations and replacements, or replacement of the furniture and equipment not paid as part of the ordinary maintenance and operation of the institutional system.

### 2.5. Disposition of Residual Funds in the Revenue Fund

At the close of each fiscal year and after all transfers and maximum deposits described above have been made, and after any deficiencies in any such transfers and deposits which may exist from any previous fiscal year have been remedied, the balance of any excess funds in each revenue fund then remaining may be used by the Board:

2.5.1. To redeem, on the next interest payment date, the bonds of the related Institution then outstanding, which are subject to redemption prior to maturity,

2.5.2. For any expenditures, including the payment of debt service, relating to improving or restoring any existing facilities of the related Institutional System, and

2.5.3. For any other lawful purpose of the related institutional system.

### 2.6. Pledges of Revenues and Income

The bonds of an institution are payable from and secured by a pledge of and lien on the following sources in the following order of priority:

- The net revenues of the related institution;
- Debt Service Reserve of the related institution, if applicable to such series of bonds;
- Uncommitted funds of the RRR account for the related institution;
- Net revenues of the other institutions, but only after provision for payment of interest due on the next interest payment date and one-half of the principal due on the bonds issued on behalf of such institution within the succeeding 12 months;
- Uncommitted funds in the RRR of the other institutions, in an amount and from such institutions as determined by the Executive Director; or
- Such other funds which may be pledged or used as authorized by the Act.

### **3. Continued Requirements**

- 3.1. Each institution shall notify the Board at least 30 days prior to each interest or principal payment date either:
  - That it has sufficient net revenue available from the institutional system to make the interest and principal payment on such payment date, or
  - That it does not have sufficient net revenues available from the institutional system to make the interest and principal payment, specifying the amount of such deficiency.
- 3.2. The rates, rents, charges, and fees (including the General Activity Fee) chargeable to the occupants of, and students, faculty members, and others using or being served by the system, shall be fixed and revised from time to time so that the:
  - Ratio of Net Revenues to Annual Debt Service in each fiscal year shall be at least equal to 120% of the Annual Debt Service for each fiscal year; and
  - The ratio of Net Revenues of each institutional system to Annual Debt Service of the bonds of that Institution in each fiscal year will be at least 120% of the Annual Debt Service for such fiscal year.
  - Failure to satisfy the rate covenant will not cause a default event if the Board engages an independent management consultant within 30 days to prepare a report with recommendations for meeting the required coverage ratio. The report will be prepared within 45 days of engagement. The Board, to the extent legally permissible, will implement the consultant's recommendation.
  - In no event may the coverage described above fall below 100% of Annual Debt Service on all bonds in each fiscal year.
- 3.3. The Board must maintain property and casualty and liability insurance as recommended by an independent insurance consultant at least once a year. The Board may self-insure subject to periodic review by an independent actuarial consultant and maintenance of funding at levels recommended by the consultant.

- 3.3.1. In the event of an insurable event, the proceeds from any insurance related to the event will be credited to the RRR account to be used to reconstruct, repair, or rehabilitate the part of the institutional system damaged.
- 3.4. The Board will provide the following via posting on the EMMA website:
- A copy of any annual or period report with respect to the System prepared for the Board;
  - A notice of any threatened termination of any accreditation material to the activities of an Institution or the commencement of any litigation or other governmental or judicial proceeding in which an outcome adverse to the Board could result in a judgment in excess of available insurance coverage within five business days after the Board has such knowledge;
  - Within 270 days of the end of the fiscal year, or as soon as available, a copy of the Comprehensive Annual Financial Report (CAFR) for the State of South Dakota;
  - Within 270 days of the end of the fiscal year, a copy of the unaudited financial statements for each Institution;
  - Unaudited Financial Statements of the Housing and Auxiliary Facilities System Revenue Bond Funds will be provided upon completion;
  - Audited Financial Statements, if and when prepared by the Board, will be provided within 30 days after availability to the Board. Audited Financial Statements are not currently prepared, and
  - By the end of October, the historical and projected worksheet for the system.
- 3.5. If any part of the information described in Section C.2.4 above can no longer be generated because the operations to which it is related have been materially changed or discontinued, the Board will provide a statement to such effect as part of its filing for the year in which such event first occurs.
- 3.6. Reportable events will be disseminated by the Board not more than 10 business days after occurrence via the EMMA website. Reportable events are:
- Principal and interest payment delinquencies;
  - Non-payment related defaults, if material;
  - Unscheduled draws on debt service reserve reflecting financial difficulties;
  - Unscheduled draws on credit enhancements reflecting financial difficulties;
  - Substitution of credit or liquidity providers, or their failure to perform;
  - Adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposal Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the security, or other material events affecting the tax-exempt status of the security;

- Modifications to the rights of security holders, if material;
- Bond calls, if material, and tender offers;
- Defeasances;
- Release, substitution or sale of property securing repayment of the securities, if material;
- Rating changes;
- Bankruptcy, insolvency, receivership or similar event of the Board;
- The consummation of a merger, consolidation, or acquisition involving the Board, or the sale of all or substantially all the assets of the Board, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and
- Appointment of a successor or additional trustee or the change of name of a trustee, if material.

#### **4. Addition/Removal of Project from the Institutional System**

- 4.1. The description of a project may be supplemented or amended at any time by the Board without the consent of a bondholder, as long as the facilities are authorized by State Statute and upon receipt of a favorable opinion of bond counsel with respect to such supplement or amendment.
- 4.2. Prior to the use of bond monies for the supplemented or amended project and if the facilities to be so included are not already part of the institutional system, the Board shall adopt a resolution which describes the new facilities and include the facilities in the Institutional System.
- 4.3. No property, plant, and equipment that is used to generate net revenue may be sold or otherwise disposed of unless:
  - The property, plant, and equipment is obsolete or worn out
  - Fair market value is received in return, or,
  - The market value of all property, plant, and equipment disposed of in any fiscal year does not exceed five percent of the total market value of all such property, plant, and equipment.
- 4.4. Prior to the removal of property, plant and equipment from the institutional system, the Board shall adopt a resolution which describes the facilities being removed and the reason of such removal.
- 4.5. No accounts receivable that are a source of net revenues may be sold, pledged, factored, or otherwise disposed of under any circumstances.

#### **5. Educating Staff Involved in Institutional System Reporting**

Each institution's Chief Financial Officer will inform his/her staff of the Board's policies and procedures for financial reporting of the Institutional System and monitor compliance.

**FORMS / APPENDICES:**

None

**SOURCE:**

BOR June 2012; March 2017; June 2018.