Frequently Asked Questions

Q1: What is the Internal Lending Program?

A1: The Internal Lending Program ("ILP") takes a portfolio approach to managing debt to minimize the cost of capital and to better manage financial risks while providing long-term fixed internal loan rates to individual institutions. The ILP allows the U. T. System to better diversify risk across the entire debt portfolio versus having each institution bear all market risk based on market conditions at the time of issuance.

Q2: When was the ILP implemented?

A2: The ILP was authorized by the Board of Regents on November 5, 2015 and is applicable for all loans after September 1, 2015.

Q3: What debt programs are proposed to be included in the ILP?

A3: The ILP is used to finance the same type of projects previously financed with RFS debt. PUF debt and TRB debt are not included in the ILP. U. T. System institutions can enter into loans with the ILP where they receive loan proceeds for capital projects and are charged periodic principal and interest amounts based on a set internal loan rate.

Q4: What loan rate will be charged on equipment financing?

A4: The interest rate on all equipment financing loans ("Short-Term Rate") through the ILP will be set at actual commercial paper rates + 0.75%. System Administration will cover all costs of issuance and ongoing costs, including liquidity costs, remarketing and dealer fees, issuing and paying agent fees, rating agency fees, and bond counsel fees. By comparison, the Texas Public Finance Authority charges an administrative fee of 1.00% on top of actual commercial paper rates. The first principal payment on short-term loans used to finance capital equipment should occur within one year of loan origination.

Q5: What interest rate will be charged on short-term loans through the ILP?

A5: The interest rate on short-term loans ("Short-Term Rate") on interim financing of capital projects will be based on the average commercial paper rate for the preceding quarter plus 0.75%, initially. Previously, dealer fees, issuing and paying agent fees, rating agency fees, bond counsel fee and other fees associated with the commercial paper program were specifically tracked and allocated across all outstanding projects financed with commercial paper. These fees will no longer be separately passed through to institutions but will instead be absorbed by the ILP.

Q6: What interest rate will be charged on long-term loans through the ILP?

A6: The interest rate on all long-term loans ("Long-Term Rate") on capital projects financed through the ILP will initially be set at 4.50%. Unlike the previous process where institutions bore the risk of market conditions at the time of pricing, the ILP loan rate is projected to be very stable. While it is projected to be stable, it is possible the Long-Term Rate could be increased or decreased in future years.

Q7: What happens to existing long-term RFS debt previously issued to finance projects?

A7: All projects previously financed with long-term RFS bonds (prior to September 1, 2015) are "grandfathered" into the System's ILP to be cash flow neutral on an annual basis and are not subject to rate changes. To better align with the ILP, however, the timing of the repayment of debt was changed from semi-annually to quarterly. Any future changes to the internal loan rate will not apply to grandfathered loans.

Q8: Can existing long-term RFS debt that has been "grandfathered" be prepaid prior to the scheduled maturity?

A8: Because existing debt was grandfathered at the inception of the ILP, the cost to prepay existing debt will be determined by either the cost to defease or redeem the underlying bonds then outstanding or the present value of the future debt service payments that were grandfathered at inception.

Q9: Can ILP long-term loans be prepaid prior to the scheduled maturity?

A9: Yes. Institutions can prepay ILP long-term loans at par on any loan repayment date with at least one month's notice in writing to the Office of Finance. For example, if the institution plans to prepay the loan on August 1st, the Office of Finance must be notified by July 1st.

Q10: Can new short-term loans be prepaid prior to conversion to a long-term loan? Can equipment loans be repaid ahead of schedule?

A10: Yes. Institutions can prepay new short-term capital loans at par with at least one week's notice in writing to the Office of Finance. Institutions should notify the Office of Finance at the same time that wire transfer amounts are due for project cost requisitions (typically, around the 15th of the month).

For equipment loans, Institutions can request repayment amounts higher than scheduled as a part of the quarterly equipment request process.

Q11: What about projects that will not comply with private business use restrictions or otherwise cannot be financed with tax-exempt debt?

A11: A flexibility premium will be added for projects that cannot be financed on a tax-exempt basis. This premium will be set initially at 0.75% (the "Taxable Premium") but may be adjusted depending on market conditions. The additional premium is needed as these projects will initially be financed with taxable debt.

Q12: What about projects previously financed with Build America Bonds ("BAB"). Will my institution continue to receive credit for the BAB interest subsidy?

A12: Projects previously financed with BABs will continue to pay only the net amount of debt service reflecting the difference between taxable debt service due to bondholders less the adjusted BAB interest subsidy (35% of interest cost reduced by the 2016 sequester reduction percentage of 6.8%). Any changes to the reduction related to the sequester subsequent to 2016 will be absorbed by the ILP, so these loans are effectively grandfathered and not subject to change.

Q13: What happens to savings generated by refunding transactions?

A13: Refunding savings that may be generated in the future will be incorporated into the ILP and factored into the determination of the internal loan rate.

Q14: What is the timing of loan payments from institutions to the ILP?

A14: Loan payments are due quarterly (11/1, 2/1, 5/1 and 8/1) beginning November 1, 2015.

Q15: When will capital project loans convert from short-term loans to long-term loans?

A15: At least one quarter after a project reaches substantial completion, the rate on the outstanding loan will convert from the Short-Term Rate to the Long-Term Rate, and principal repayment will commence. Substantial completion dates will be reviewed quarterly in connection with the CIP update (i.e. February, May, August, November). For example, a project that reaches substantial completion in March will be reflected as being substantially complete in the May quarterly review; after one full quarter, the loan rate will be converted to the Long-Term Rate effective August 1, with the first payment at the Long-Term Rate due November 1. The first principal payment on long-term loans should generally occur within one year of substantial completion and will generally being on the first Long-Term Rate payment date.

Q16: Will the Long-Term Rate be stable?

A16: Yes. The Long-Term Rate is expected to be very stable. By utilizing a portfolio approach to manage risk, it is expected that the Long-Term Rate will not need to be adjusted; however, substantial changes in the interest rates in the capital markets over time could result in the need to change the internal loan rate, which would be applied across all ILP long-term loans. Changes could involve either increases or decreases to the Long-Term Rate.

Q17: How frequently will rates change?

A17: Although it is not expected to change frequently, if a change in the rates is needed, the change will be communicated to the institutions during the annual budget process. Rates that are subject to change are (1) the Long-Term Rate, (2) the premium charged over the Short-Term Rate, and (3) the flexibility premium for projects that are unable to be financed with tax-exempt debt (the “Taxable Premium”).

Q18: How will my institution receive loan proceeds?

A18: The reimbursement process will be largely unchanged. Institutions will continue to be reimbursed on capital projects financed with RFS debt through the standard OFPC monthly construction reimbursement process. The Office of Finance will ensure sufficient loan proceeds are available to reimburse institutions on the monthly reimbursement date. Equipment financing will continue to be processed on a quarterly reimbursement basis up to the annual amount of RFS Equipment Financing authorized by the Board of Regents for each institution.

Q19: How will each loan be evidenced?

A19: Each loan will be evidenced by a promissory note/term sheet that will be executed following Board approval of the authorized amount of RFS financing. If necessary, the loan amount will be reduced once the project is closed out pursuant to OFPC's Form 4/5 formally reducing the amount of authorized RFS debt. Annually, in connection the System budget process, a list of outstanding loans will be provided to each institution.

Q20: Will each capital project be charged interest on the full authorized RFS amount?

A20: No. Each project is assessed interest based only on the amount of loan proceeds provided to the institution through the monthly OFPC construction reimbursement process for capital projects or reimbursement in connection with the RFS capital equipment financing program. As a result, capital projects no longer carry an unexpended proceeds balance and earn interest income, as done prior to the establishment of the ILP, as balances are longer invested for specific projects.

Q21: What amortization terms are available for short- and long-term loans?

A21: The amortization terms for short- and long-term loans are unchanged. Short-term loans for capital equipment range from 3-10 years depending on the useful life of the capital equipment. Long-term loans are amortized over 10-30 years depending on the useful life of the capital project.

Q22: What costs can be reimbursed for equipment loans?

A22: Capital equipment is generally regarded as nonexpendable, tangible personal property having a useful life of more than one year. The acquisition cost for equipment includes the net invoice price, including any modifications, attachments, accessories, or auxiliary apparatus necessary to make it usable for the purpose for which it is acquired. In addition, taxes, duty, in-transit insurance, freight, and installation charges are also included as part of the acquisition cost. Capital equipment, including software, that will be used systemwide, or between and among U. T. institutions and System Administration, is eligible for RFS Equipment Financing.

Additionally, any capitalized costs associated with the development or implementation of software, including personnel costs (salaries), are eligible for RFS Equipment Financing if they are incurred in the Application Development Stage. This principle applies whether the salaries are paid to employees of the institution or to outside parties. See UTS 142.13 Accounting and Financial Reporting for Intangible Assets at http://www.utsystem.edu/bor/procedures/policy/policies/uts142_13.html. Training costs related to software usage are discussed below.

The purchase of bundled software included as part of the initial acquisition of computer hardware is capitalizable regardless of threshold and therefore eligible for RFS Equipment Financing.

Software maintenance costs are considered operating expenses and therefore are not eligible for RFS Equipment Financing as these are considered operating expense.

Costs for software licenses with a useful life extending beyond one year that will be owned are eligible for RFS Equipment Financing. Leased or licensed software that requires the payment of an annual fee (i.e., does not have a useful life extending beyond one year) and that will not be owned when the license expires is not eligible for RFS Equipment Financing.

Q23: What costs cannot be reimbursed for equipment loans?

A23: The cost of warranties and similar service features related to a purchase of capital equipment (such as maintenance agreements and loaner programs) are not eligible for RFS Equipment Financing as these are considered operating expenses. This ineligibility also applies to warranty and similar service feature costs separately identified during original purchase. For example, a warranty agreement charge that is separately identified on a Laptop purchase is not allowed.

Employee training and travel costs are not eligible for RFS Equipment Financing as these are considered operating expenses.

Consumables, which generally include those items that have an expected useful life of less than one year, are not eligible for RFS Equipment Financing as these are considered operating expenses. Some examples include, but are not limited to: chemicals, gases, paper, staplers and other office supplies, toner cartridges, medical supplies, disposal services, and laboratory supplies.

Examples of other operating expenses that are not eligible for RFS Equipment Financing include, but are not limited to: monthly telephone services, animals, software maintenance cost, and routine maintenance.