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DEPARTMENT OF BUDGET AND FINANCE

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ADMINISTRATIVE AND RESEARCH OFFICE
BUDGET, PROGRAM PLANNING AND
MANAGEMENT DIVISION
FINANCIAL ADMINISTRATION DIVISION
OFFICE OF FEDERAL AWARDS MANAGEMENT (OFAM)

March 12, 2019

FINANCE MEMORANDUM

MEMO NO. 19-03

TO: All Department Heads

FROM: Roderick K. Becker 
Director of Finance

SUBJECT: General Obligation Tax-Exempt Bonds
Use of Bond Proceeds

The Department of Budget and Finance (B&F) would like to remind all departments and agencies of the State of Hawai'i (State) of certain regulations related to the use of tax-exempt General Obligation (G.O.) bonds. G.O. bonds, which are appropriated by the Legislature, are typically used to finance capital improvement projects throughout the State. These appropriations are funded by the State through the issuance of tax-exempt G.O. bonds.

In order to preserve the tax-exemption on the bonds, the State is required to comply with numerous federal tax requirements. Failure to comply with federal tax law can jeopardize the tax-exempt status of the bonds and have significant adverse consequences on the bondholders. Accordingly, B&F would like to ensure that all departments and agencies utilize their G.O. bond appropriations to pay for only **eligible** capital expenditures relative to the acquisition, construction or improvement of property. Please be advised that G.O. bonds cannot be used to pay for costs such as operating costs, routine maintenance of buildings or equipment, payments made pursuant to service contracts, and any item of property which is not capitalizable.

To assist departments and agencies with their determination of eligible capital expenditures, B&F has prepared, with the assistance of the State's General Advice Counsel, a "Summary of Costs Eligible and Not Eligible for Payment with Tax-Exempt Bond Proceeds" (see Exhibit A). Departments and agencies are advised to contact B&F should questions arise regarding specific costs not addressed in Exhibit A.

Should you have any questions, your staff may call the Financial Administration Division's Administrator at 586-1612.

Attachment

EXHIBIT A
State of Hawaii
General Obligation Tax-Exempt Bonds

Summary of Costs Eligible and Not Eligible for Payment with Tax-Exempt Bond Proceeds

This summary is intended as a brief and general guide of costs eligible and not eligible for payment with tax-exempt bond proceeds. This summary focuses on general types of expenditures and does not address questions such as private use of financed property. **Users of this Summary should contact the Department of Budget and Finance if questions arise concerning specific costs that are not addressed below.**

I. Capital Expenditures are Eligible for Tax-Exempt Financing

A. In General: capital expenditures are any costs chargeable to the capital account of an asset, such as costs to acquire, construct, or improve land, buildings and equipment.

B. Examples of Capital Expenditures for the Acquisition of Property:

1. Bidding costs;
2. Invoice Cost;
3. Shipping fees and delivery costs;
4. Negotiating the terms of acquisition;
5. Preparing and reviewing the bid, offer, or purchase agreement;
6. Installation Costs;
7. Examining and evaluating title;
8. Securing permits;
9. Conveyance costs including sales and transfer taxes and title registration;
10. Broker's commissions;
11. Fees for architectural, geological, survey, engineering, environmental or inspection services;
12. Costs to acquire intangible real property interests, such as leaseholds or easements;
13. Amounts paid to renegotiate a lease, or, where the governmental unit or agency is the lessor, to terminate a lease of real or tangible personal property; and

C. Examples of Expenditures Paid to Construct or Improve Property:

1. In general: all direct or indirect costs that directly benefit or are incurred by reason of the construction or improvement;
2. Cost of removing a building system or building component as part of a replacement project;
3. Amounts paid for the betterment of property, e.g., enlargement, expansion, extension, or addition of major component or material increase in capacity or amounts paid to materially increase productivity, efficiency or output, or amelioration of material condition or defect existing prior to acquisition or arising during construction;
4. Amounts paid to restore damage to property;
5. Amounts paid to restore nonfunctional property to its ordinarily efficient operating condition or that result in the rebuilding of the property to a like-new condition;
6. Amounts paid to adapt property to a new or different use;
7. Specific Categories of Costs:
 - a. Architectural, engineering, design, surveying, soil testing and other site investigation and preparation;
 - b. Amounts paid under contracts for construction, renovation, improvement;
 - c. Direct labor costs of employees allocable to work related to the construction or improvement;
 - d. Indirect costs that directly benefit or are incurred by reason of the construction or improvement work, such as:
 - i. Indirect labor costs (including pension and other employee benefit expenses allocable to the work);
 - ii. Cost of renting or leasing property used in the performance of construction or improvement work;
 - iii. Bidding costs for solicitation of contracts; and
 - iv. Onsite storage and security costs

II. **Costs Not Eligible for Tax-Exempt Financing: Working Capital Costs.** Such costs include:

- A. All overhead and administrative costs identified with a department or function not generally allocable to construction or production, such as financial accounting, financial planning, insurance or risk management, environmental management, personnel policy;
- B. Operating costs, such as employee salaries and benefits, utilities, materials costs, rental costs, in each case not related to or incurred by reason of activities related to the acquisition, construction or improvement of real or personal property;

C. Routine maintenance of buildings or equipment, i.e. recurring activities expected to be performed as a result of use of the building or equipment in order to keep the property in its ordinary efficient operating condition. Routine maintenance includes inspection, cleaning, testing, replacement of worn parts with comparable and commercially available replacement parts;

D. Payments made pursuant to service contracts, such as IT service contracts;
and

E. Any item of property which is not capitalizable.