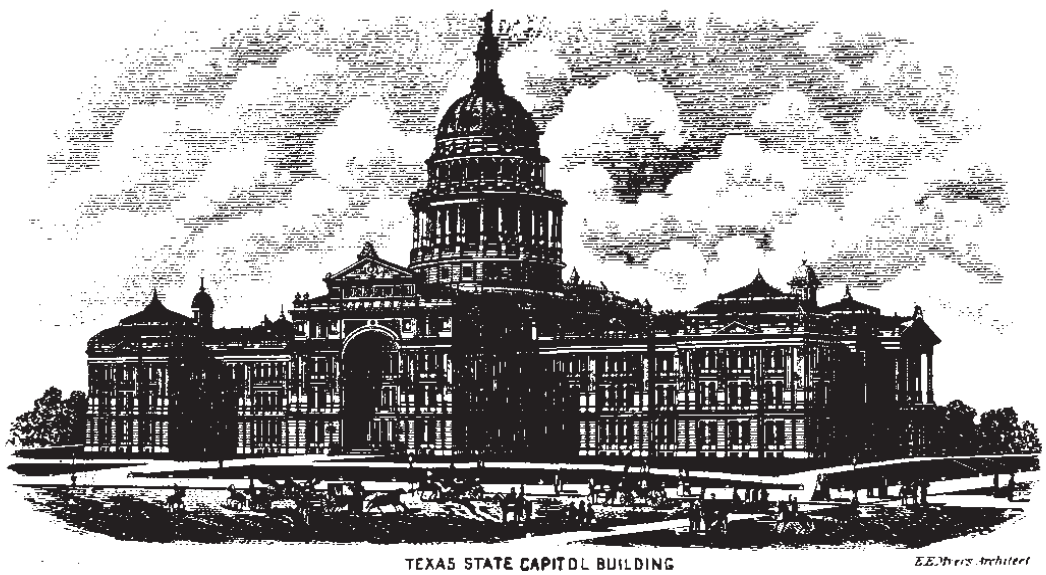
Sunset
Advisory Commission



Texas Hospital Equipment Financing Council

Staff Report

1998

SUNSET ADVISORY COMMISSION

In 1977, the Texas Legislature created the Sunset Advisory Commission to identify and eliminate waste, duplication, and inefficiency in government agencies. The 10-member Commission is a legislative body that reviews the policies and programs of more than 150 government agencies every 12 years. The Commission questions the need for each agency, looks for potential duplication of other public services or programs, and considers new and innovative changes to improve each agency's operations and activities. The Commission seeks public input through hearings on every agency under Sunset review and recommends actions on each agency to the full Legislature. In most cases, agencies under Sunset review are automatically abolished unless legislation is enacted to continue them.

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Review Summary

Review Summary

The purpose of the Texas Hospital Equipment Financing Council is to preserve the validity and enforceability of the bonds of the Council that were outstanding on September 1, 1989. The Council is mandated to provide for the bond payments until the bonds are discharged or adequate provisions for the bonds are made. Originally, the Council had a much broader mandate. It was responsible for providing health related equipment financing at a reasonable cost to small rural hospitals. Included in its mandate was the power to issue, sell and deliver bonds to pay for health-related equipment, refund outstanding bonds, and pay premiums and interest on outstanding bonds. However, since 1989, the Council has had a more limited function.

From its initial review of the Council's Self Evaluation Report, Sunset staff realized that the Council had almost accomplished its limited purpose and that its continued existence might not be necessary. Over the past several years, the Council's Board of Trustees has met rarely or not at all. The Board only meets to formally approve the actions of the bond trustees which are reported in the Council's Annual Financial Report. Board members have not been reappointed in the past 10 years and all members are serving expired terms. The Council has no staff or office. Staff from the Comptroller's Office act as the agency contact and provided assistance for the Sunset review. Sunset staff learned early in the review that the single loan holder of the Council planned an early payoff of its loan and that would lead to the redemption of all remaining bonds of the Council.

The Council had a limited purpose that has been accomplished.

In conducting the review of the Council, the Sunset staff:

- worked with Comptroller's Office support staff;
- reviewed agency documents and past State Auditor reports;
- reviewed current statutory provisions providing for the financing of hospital equipment;
- received information from interest groups;
- interviewed staff of bond trustee; and
- reviewed past legislation.

Abolishing the Council will not effect public hospitals' ability to issue bonds to pay for equipment needs.

Because of the limited powers and duties of the Council, the Sunset review focused solely on the need for the Council after the bonds were paid. Once Sunset staff determined that the bonds and interest had been paid, staff concluded that the agency should not be continued. The Council's enabling statute provides for this inevitability and staff found no reason to alter this course. Abolishing the Council would not eliminate any privilege currently enjoyed by public hospitals to issue bonds to finance their equipment needs.

Issue

Issue 1

Abolish the Texas Hospital Equipment Financing Council.

Background

In 1983, the Legislature created the Texas Hospital Equipment Financing Council to provide low-cost loans to public and private hospitals, especially in rural areas, for the purchase of hospital equipment.[1] Hospital authorities and other public entities may issue bonds to finance the construction of hospitals and the acquisition of equipment.[2] Since the interest on those bonds is exempt from federal income tax, the cost of borrowing is generally 3 to 5 percent less than conventional loans. When the Council was created, many small to mid-sized hospitals could not take advantage of this tax-exempt financing because of the high cost of issuing the bonds. The Council was intended to provide small hospitals access to this funding source.

The Council was created to provide small hospitals access to low cost funding.

Although one small hospital's equipment needs might not justify the expense of issuing a bond offering, when the equipment needs of small hospitals for the entire state are pooled, the bond approach to financing becomes more feasible. The Legislature's intent was to have the Council issue, sell, and deliver revenue bonds to pay for health care equipment needs of the entire state. Small hospitals would borrow from the Council and receive the benefit of the lower financing cost while the expense of bond issuance would be shared by a number of these small hospitals.

In 1989, the Legislature reacted to the low lending rates of the Council by limiting its responsibilities to fulfilling its outstanding bond obligations and by taking away the Council's authority to issue new bonds. The Legislature found that by 1985 the Council had sold $62.2 million in bonds and lent only about 45 percent of those funds.[3] The text box, *Loans Made by the Hospital Equipment Financing Council*, shows the three loans made by the Council, when they were made, the loan amount and when they were repaid. Because the interest earned on the outstanding loans was insufficient to pay off the bonds at their redemption due date, the maturity date of the bonds had to be extended in the summer of 1988 to prevent a default. As a result of these problems, all remaining bonds – not secured by one of the Council's three loans – were paid off.[4]

In 1989 the Legislature also reduced the size of the Council's board from 12 to three members and made the State Treasurer the Council's official custodian and required it to provide staff support. In 1997, the Legislature shifted this responsibility to the State Comptroller.

Loans Made by Hospital Equipment Financing Council

Borrower	Date of Loan	Amount	Date of Repayment
Valley Baptist Medical Center (Harlingen, Texas)	August 31, 1987	$2,500,000	May 20, 1998
Valley Baptist Medical Center (Harlingen, Texas)	January 6, 1988	$2,100,000	May 20, 1998
Baptist Memorial Hospital Systems (San Antonio, Texas)	August 1, 1988	$23,084,678	November 28, 1990

Policymaking Body

Board of Trustees members have not been appointed in more than 10 years.

The Council's enabling statute provides for the Council to be overseen by a three-member Board of Trustees. However, members have not been appointed to the Board in more than 10 years. The text box, *Hospital Equipment Financing Council Board of Trustees*, shows the Board members who continue to serve even after the expiration of their terms.

Hospital Equipment Financing Council Board of Trustees

Current Board Member	Appointment Date	Term Expiration
Dan Patterson, Chair	February 4, 1988	September 1, 1993
Calvin Person, Vice-Chair	November 20, 1987	September 1, 1993
Richard F. Kiepfer, M.D.	September 24, 1987	September 1, 1993

The statute charges the Board with preserving the validity and enforceability of the bonds that are outstanding on September 1, 1989.[5] The Board, however, does not carry out any duties with respect to daily operations or activities of the Council. It has oversight authority over the proceeds from the revenue bonds issued by the Council back in the 1980's. The Board usually meets once a year to approve the Annual Report. The text box, *Meetings of the Hospital Equipment Financing Council Board of Trustees*, shows the Board meetings for the past 10 calendar years. The Board did not meet in 1996 and met just once in 1997, by tele-conference.

Meetings of the Hospital Equipment Financing Council Board of Trustees

January 1987 to December 1990	12 Meetings
January 1991 to December 1996	11 Meetings
January 1997 to Present	1 Meeting (by Telephone)

Funding

The Hospital Equipment Financing Council does not receive an appropriation from the Legislature. The Council has a limited amount of available funds through the bond agreement to pay for allowable expenses, such as travel expenses incurred by Board members. Available funds consist of the difference between interest earned on loans made and the interest owed on issued bonds. Board members submit their expenses to the bond trustee who can make payment from available funds. The Comptroller of Public Accounts provides staff support necessary to carry out the Council's responsibilities from existing resources.

Operations

The Council does not perform any day-to-day activities. The Bank of New York, Trust Company of Florida, N.A. (trustee) acts as trustee for the outstanding loans. The trustee reports its activities to the Comptroller's office, including receiving loan payments, making bond payments, compiling reports on loan payments received, and bond payments made on behalf of the Council. The Comptroller's Office is then responsible for preparing the Annual Financial Report for the Council and presenting it to the Board of Trustees for its approval. The Comptroller's duties also include maintaining Council records, and arranging necessary Board meetings.

Sunset Review

The Sunset staff evaluated the continuing need for the Hospital Equipment Financing Council. As required by the Sunset Act, to justify a continued need for an agency, certain criteria must be met. Key criteria include identification of the objectives intended for the agency, the problem or need the agency was intended to address, and the extent to which those objectives have been achieved.[6]

Findings

The Council has had limited success providing loans to small hospitals.

▼ **The Council never fulfilled the Legislature's expectations for providing financing for hospital equipment.**

◗ From its inception, using the Council to finance hospital equipment has had limited success. The company insuring the bonds had approval authority over any loans made by the Council. The target groups for the Council loans were the small rural hospitals, many of which had little or no credit histories. For most, if they did have a credit history, it was a poor one. Because of their credit characteristics, many of the Council's target groups of hospitals could not qualify for loans under the insuring company's guidelines. The Council therefore had a limited number of qualified applicants for their loans.

In 1989, the Legislature eliminated the Council's authority to issue new bonds.

- During the early to mid 1980's small and rural hospitals were experiencing economic problems. Many of these hospitals were either closing their doors or cutting back on expenses because of cash flow problems. These problems limited or prohibited the hospitals from assuming more debt even if they could meet the insuring company's qualifications.[7]

▼ **The Legislature responded to the Council's lack of success by limiting its powers and duties.**

- In 1989, after finding the Council had only been able to loan 45 percent of its bond money, the Legislature limited the Council's responsibilities to fulfilling its outstanding bond obligations and eliminated the Council's authority to issue new bonds. As a result, the Council only exists to preserve the validity and enforceability of the Council's bonds that were outstanding as of September 1, 1989.

- In addition, the Legislature amended the Sunset provision for the Council to remain in existence only until the bond obligations were paid, discharged, or adequately provided for.

The Council no longer serves a needed purpose.

▼ **The Hospital Equipment Financing Council is no longer needed.**

- On July 31, 1998, the trustee notified the Council that all outstanding loans made by the Council have been repaid, and that it intended to redeem all outstanding revenue bonds.

- On October 7, 1998, the Council's bonds that were outstanding on September 1, 1989 were finally redeemed. The Council has completed its obligations relating to these bonds and no longer serves a needed purpose.

Conclusion

The Council was created as a means for small rural hospital to have access to bond financing for their equipment needs. Because of economic problems with the targeted groups, the Council never enjoyed the success its proponents envisioned. In 1989, the Legislature limited the Council activities to ensuring that the validity and enforceability of all outstanding bonds was maintained. Since all bonds have been redeemed, the Council no longer serves a needed purpose.

Recommendation

- **The Hospital Equipment Financing Council should be abolished under the terms of the Sunset Act.**

Under this recommendation, no action would be needed by the Sunset Commission and no legislation would be needed to abolish the Council. The Council would simply be abolished on its Sunset date of September 1, 1999. Because the bonds that were outstanding on September 1989 have been paid, the standard one-year period for an abolished agency to conclude its affairs would be unnecessary.

Fiscal Impact

This recommendation would have no fiscal impact to the State because the Hospital Equipment Financing Council receives no State funding. All outstanding bonds have been redeemed.

[1] Tex. S.B. 752, 68th Leg. 1983. (Now codified in Texas Health and Safety Code § 224.001 et seq.).

[2] Hospital Project Financing Act, Texas Health and Safety Code § 223.001 et seq.

[3] The bill analysis for S.B. 1387 reported that 60 percent of the bond money had been loaned out. However, financial records of the Hospital Equipment Finance Council show that only three loans, totaling approximately $27.7 million, were made. This would be about 45 ;ercent of the $62.2 million bonds sold.

[4] House of Representatives, Public Health Committee, *Bill Analysis* S.B. 1387, Seventy-first Legislature.

[5] Tex. Health & Safety Code § 224.051(a).

[6] Texas Sunset Act, Tex. Gov. Code § 325.011(2).

[7] Ibid.

Texas Hospital Equipment Financing Council

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