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News Release

PBC receives material rating increase for SCKMC bond refinancing

Public Building Commission refunding bonds receive 'A' rating, stable outlook

ARKANSAS CITY, Kan. (May 17, 2019) — City of Arkansas City officials were notified Wednesday by S&P Global Ratings that the Ark City Public Building Commission's refunding revenue bonds, Series 2019, estimated at \$19.035 million, will be assigned a bond rating of "A," with a stable outlook.

The Public Building Commission (PBC), which is composed of the five city commissioners and four other members of the public, is the entity that issued the debt service for South Central Kansas Medical Center's (SCKMC) new facility, which opened in March 2011 in Patterson Park Subdivision.

The original \$23.205 million in hospital financing was secured by an unconditional lease payment from the City, supported by its issuance of revenue bonds. SCKMC currently is responsible for making annual bond payments through its net revenues, with the aid of the one-cent Health Care Sales Tax.

This new A-stable rating for the refinancing of the original revenue bonds is essentially four steps better than when the original bonds were issued in 2009, when they were rated Baa3 by Moody's Investor Service. More recently, Moody's had rated those original bonds as B2, with a negative outlook — meaning A-stable would be a comparative improvement of nine steps for the 2019 bond refinancing.

The upgrade to "A" reflects citizens' approval of a new revenue source to support ongoing subsidies of SCKMC for debt service and potential refinancing. Specifically, the upgrade reflects the 2018 passage of the 1-percent Health Care Sales Tax to cover the medical center's debt service payments.

"Many factors went into receiving this rating," said City Manager Nick Hernandez, "from passage of the new sales tax, with no sunset, to the significant financial turnaround — led by CEO Jeff Bowman and his staff — of SCKMC, which previously had contributed to the wariness displayed by the current rating."

SCKMC Chief Executive Officer Jeff Bowman agrees that word of the new rating is very good news for Arkansas City taxpayers. "Nick Hernandez initiated the work that led to this great news," he said.

For immediate release

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“The groups that he set up worked really well with the City and the hospital staff to bring this about. We are greatly indebted and appreciate the local voters who approved the one-cent sales tax last year.”

That approval was the keystone in obtaining this improved rating. Hernandez and Bowman said that without that new tax vote, this refinancing would not now be possible.

“It’s really a great example of local citizens believing in something and being willing to shoulder the cost,” Bowman said. “Clearly, it helps the hospital and it helps the community retain its own local medical center. Beyond that, if things proceed as expected, it will save us all millions of dollars in the long run.”

The Health Care Sales Tax, the collection of which began Jan. 1, will allow SCKMC to become more financially solvent in the long term by removing the debt burden from the medical center.

“With the first-quarter financial report showing the hospital operating in the black for the first time in three years, the combination of improved finances and a potentially much lower interest rate suggests a brighter future for the hospital, the City of Arkansas City, and the entire community,” Bowman said.

Of the 2018 Health Care Sales Tax revenues, 95 percent is pledged directly toward the bond payments, supplemented by additional City appropriations in an amount equal to the other 5 percent.

“We anticipate significant savings over the existing finance structure and debt issuance,” Hernandez said. “With those savings, we project this debt could be paid off sooner than even the original issuance.”

The original bonds were scheduled to be paid off in 2038. The refunding bonds, Series 2019, will be dated July 23, 2019, and are due September 1, 2044, but City officials anticipate paying them off significantly sooner, depending on the final outcome of the bond sale.

The City will utilize the proceeds from the 1-percent Health Care Sales Tax to make the debt payments. The Series 2019 bonds are special, limited obligations of the PBC, which will be payable from a trust estate. All committed revenues will be deposited with a third-party trustee. Excess revenues over the debt service payments will remain in the third-party trust account, separated from City funds, to aid in the early payoff of the bond debt.

Once the Series 2019 refunding bonds are paid off in full, the Health Care Sales Tax could then be repealed by a future City Commission. This also was the intent of the current commission, as expressed in Resolution 2018-06-3185, which was approved June 19, 2018.

S&P: City’s financial position ‘strong’

Cities in Kansas have a strong institutional framework score, which means they have a high capacity to meet their financial commitments. Among Arkansas City’s specific strengths lauded by S&P are:

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- Strong management, with good financial policies and practices under S&P's financial management assessment methodology;
- Strong budgetary performance, with balanced operating results in the General Fund and an operating surplus at the total governmental fund level in fiscal year 2018;
- Strong budgetary flexibility, with an available cash reserve in fiscal year 2018 of 25 percent of operating expenditures;
- Very strong liquidity, with total government available cash at 92.8 percent of total governmental fund expenditures and 4.1 times governmental debt service.

Signs of life in economy

Although one of the weak points in the City's profile is what S&P terms a "very weak economy," its report notes there are many positive recent developments for Arkansas City's major industry employers.

"Despite our very weak assessment of the city's economy based on wealth and income levels, major employers have been expanding steadily," S&P notes.

"Creekstone Farms, the 12th-largest U.S. beef packer, is investing \$85 million in expansion projects. Walmart has recently selected the company as its supplier as it enters into the beef industry, developing an end-to-end supply chain for Angus beef. This is expected to add more than 250 jobs to Arkansas City, and beef produced at the Creekstone facility will be sold in 500 Walmart stores ... in the Southeast."

"KanPak's Arkansas City location is the largest in the U.S., serving hundreds of restaurants and retail stores, including Chick-fil-A, Whataburger, Tim Horton's, QuikTrip, 7-Eleven and Perrigo," the S&P report adds. "The company, owned by Golden State Foods, recently opened a 200,000-plus-square-foot, \$16 million packaging and distribution facility in the city. In addition, it's investing \$60 million in improvements to its manufacturing plant..."

S&P also noted the relative strength of Strother Field Airport and Industrial Park, which accounts for 47 percent of the total economic output of all general aviation airports in Kansas, as well as 20 percent of the total economic output of all airports in the state combined (including commercial).

"The City is also experiencing residential growth, and officials note that new housing is not keeping up with the demand, given the commercial and industrial expansions and the job creation in the city," S&P concluded its economic analysis.

"Market value has increased in line with the growth of the local economy and we anticipate that these trends will continue given ongoing development, although we do not anticipate changes to the city's wealth and income levels over the outlook horizon."

Strong management and budgetary performance

S&P had positive things to say about the City of Arkansas City's financial management practices.

"We view the City's management as strong, with good financial policies and practices under our financial management assessment methodology, indicating our view that financial practices exist in most areas..." the report states.

And "Arkansas City's budgetary performance is strong, in our opinion. The city had a balanced operating result in the general fund of 0.4 percent of expenditures and a surplus result across all governmental funds of 3.1 percent in fiscal (year) 2018."

The general fund surplus in fiscal year 2018 resulted from expenditure savings in several categories, particularly a \$300,000 contingency that the City included in its annual General Fund budget.

Property taxes accounted for 26 percent of adjusted General Fund revenue, followed by sales taxes (16 percent) and franchise fees (13 percent). "The City's ad valorem and sales tax base has been a reliable revenue stream over the past five years," S&P noted.

"Arkansas City's budgetary flexibility is strong, in our view, with an available cash reserve in fiscal (year) 2018 of 25 percent of operating expenditures, or \$2.3 million. The cash reserve consists of \$945,000 (9.9 percent of expenditures) in the General Fund and \$1.4 million (14.6 percent of expenditures) outside the General Fund, but legally available for operations."

Finally, "in our opinion, Arkansas City's liquidity is very strong, with total government available cash at 92.8 percent of total governmental fund expenditures and 4.1x governmental debt service in 2018," S&P states. "In our view, the City has strong access to external liquidity, if necessary. ... Arkansas City does not have privately placed debt or contingent liabilities that could cause imminent or future liquidity pressures. Given financial projections for the current and next fiscal year, we do not believe the City's liquidity will deteriorate over the outlook horizon."

About the Public Building Commission

Composed of the five city commissioners and four other citizens, the Arkansas City Public Building Commission was created for the purpose of financing and constructing public buildings and facilities.

In 2009, based on overwhelming support from the citizens in a 2008 election question, the PBC issued \$23.205 million in revenue bonds, at a maximum interest rate of 7 percent, to construct South Central Kansas Medical Center's new 49-bed facility in Patterson Park Subdivision.

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After the Sept. 1 payment is made, about \$19.7 million in outstanding debt will remain to be paid off.

The City will use excess bond reserve and accumulated sales tax funds to reduce the size of the refinancing bond issue to \$19,035,000.

The elected members of the Public Building Commission are Mayor Jay Warren, Vice Mayor Karen Welch, Commissioner Kanyon Gingher, Commissioner Dan Jurkovich and Commissioner Duane Oestmann. The appointed members are Chairman Mike Munson, Vice Chair Angela Bruce, David Billings and Charles Tweedy III.

The commission generally meets at 5 p.m. on the third Tuesday of each September, and at other times as needed. It will meet again on June 18 and July 2 to continue the bond refinancing process.

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