

# STATE OF WEST VIRGINIA

## Workers' Compensation Division

### SPECIAL REPORT

**Options and Consequences**

**Regarding  
Lease-Purchase Agreement for  
Property at**

**601 Morris Street**

**OFFICE OF LEGISLATIVE AUDITOR**

**Performance Evaluation and Research Division**

**CAPITOL BUILDING  
CHARLESTON, WEST VIRGINIA 25305**

PE 95-08-29

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October, 1995



## Table Of Contents

Forward	iii
Part 1: The Lease-purchase Agreement Contains Provisions For Immediate Termination, Right To Cancel Clause	1
Part 2: PERD's Survey Of The States Offers Empirical Evidence That Few States Have Broken Lease-Purchase Agreements And That Negative Consequences Have Resulted For Those Who Have Done So	3
Part 3: The Secretary Of The Department Of Administration Has Had Extensive Dialog With Rating Agencies	7
Part 4: Analysis Of The Effects Of Canceling The Lease-Purchase Agreement	9
Part 5: Maintenance Is A Responsibility Of The Tenant	13
Part 6: Other Options Should Be Considered.	15
Part 7: Conclusions And Recommendations	17
Appendix A: Research Objective And Methodology	19
Appendix B: Lease-Purchase Survey	21
Appendix C: Survey Results	23
Appendix D: Correspondence From Secretary Of Administration	25
Appendix E: Correspondence From Commissioner Of Bureau of Employment Programs	27
Appendix F: Approximations Of Municipal Bonds Yields By Grade And Maturity September 1995	37



## List Of Tables

Table	Title	Page
1.	Survey Summary . . . . .	5
2.	Estimated Ranges for Bond Insurance . . . . .	12



## Foreword

On August 3, 1988, the State of West Virginia, through the Department of Finance and Administration, entered into a lease-purchase agreement with the Charleston Building Corporation for the building and property located at 601 Morris Street. At that time, the previous administration agreed to pay \$8.6 million for the property at an effective rate of 9.4% interest over 20 years. The total payments to the Charleston Building Corporation under the contract are to total \$19,080,000. An appraisal done on August 11, 1988, was issued to Mellon National Bank on October 4, 1988. The appraisal set the value of the building and property at slightly more than \$9.1 million. However, the appraised value of the building was based upon the income stream to be generated under the contract signed the previous week. The appraisal stated:

The approaches to value...are predicated upon a sole tenant being the State of West Virginia who...has evidenced its intent to lease for the next 20 years. As long as this lease continues and the State honors its commitment, these estimates are considered reasonable. **However, if the State vacates the building, then it would be difficult to find a tenant to use this much space on these terms and conditions.** (emphasis added)

It should also be noted that only 20 months earlier the building and property were sold for \$2.5 million. Thus in only 20 months, without major renovations, the value of the property, a former warehouse, jumped \$6.1 million or a 244% increase.

On February 1, 1995, the Workers' Compensation Division was moved from the Morris Street Building to the City Center East office tower in Kanawha City. The Division was moved due to the deplorable conditions at 601 Morris Street, including a serious asbestos problem, inadequate wiring, numerous fire code violations, and the simple fact that the building was designed as a warehouse not an office complex. So now in addition to the \$80,000 monthly lease-purchase payment the Workers' Compensation Division is paying on the Morris Street property, it is now also having to pay \$900,000 a year to rent City Center East.





## **Part 1: The Lease-Purchase Agreement Contains Provisions For Immediate Termination, Right To Cancel Clause**

The contract provides for the termination of the lease through both Items 11 and 13 of the agreement, *Provisions for Immediate Termination* and *Cancellation of Lease*, respectively. The provisions for termination are required by statute to ensure that the contract does not bind future Legislatures to agreements made by a sitting Legislature. The provisions are further detailed below.

Item 11, or *Provisions for Immediate Termination*, allows for the cancellation of the lease in the case that the Legislature fails to provide sufficient funds or otherwise impairs the lease, or in the event that it shall become unlawful to maintain a state facility on leased premises (*West Virginia Code §12-3-17(2)*).

Item 13 of the lease-purchase agreement which provides the state with the right to cancel the agreement reads as follows:

*It is further agreed by and between the parties hereto that the Department of Finance and Administration, as Lessee, shall have the right to cancel this lease, without further obligation on the part of the Lessee, upon giving thirty (30) days' written notice to the Lessor, such notice being given at least thirty (30) days prior to the last day of the succeeding month (12-3-17(1) West Virginia Code). (Emphasis added).*

It was required that the contract contain the *Provisions for Immediate Termination* and *Cancellation of Lease* clause by the cited statute, §12-3-17 which states the following:

*Except as provided in this section, it shall be unlawful for any state board, commission, officer or employee: (1) To incur any liability during any fiscal year which cannot be paid out of the then current appropriation for such year or out of funds received from an emergency appropriation; or (2) to authorize or to pay any account or bill incurred during any fiscal year out of the appropriation for the following year...*

Almost any state contract, including those financed by the issue of bonds, must contain similar language to be considered negotiable. The state clearly has the right to exercise a cancellation, but exercising this right may cause anxiety for bond raters, who would prefer to view compulsory cancellation clauses in state contracts as legal formalities rather than real options. The contract and state law clearly allow for the termination of the agreement, however the *invisible hand* of the market may not be as accommodating.<sup>1</sup>

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<sup>1</sup> *The impact a termination could have on the State's bond rating and future contract negotiations is detailed in other sections of this report.*

The contract also contains a nonsubstitution clause (Item 14) which is open to legal interpretation. The clause reads as follows:

*Without in any way compromising the rights under West Virginia Code §12-3-17, Lessee further represents and warrants that **except for compelling reasons of public policy as determined solely by the Commissioner of Finance and Administration of the State of West Virginia**, it will not, during the first three months following the date on which any said necessary cancellation takes effect, lease, purchase or otherwise acquire any property intended for the replacement of or substitution for the leased premises. (Emphasis added).*

It has been reported in a newspaper account that a Charleston attorney who represented the lessor and helped to draft the lease-purchase agreement explained that the nonsubstitution clause was added to soften the cancellation clause for the purpose of making the deal "as palatable as possible" to investors. The Attorney General is reported to have given the opinion that the nonsubstitution clause is void. Based upon the emphasized phrase in the contract excerpt above, the PERD believes the Secretary of the Department of Administration has the right to effectually nullify the clause.

**Part 2: PERD's Survey Of The States Offers Empirical Evidence That Few States Have Broken Lease-Purchase Agreements And That Negative Consequences Have Resulted For Those Who Have Done So**

The PERD's survey of financial officers of the other 49 states was directed to determine the feasibility of terminating the lease-purchase agreement on the property at 601 Morris Street. Initially the PERD mailed a questionnaire to each state (see Appendix B for questionnaire). Few responses were received and the remaining states were divided among all available staff, along with appropriate instruction for conducting a follow-up telephone survey in an attempt to gain a 100% response rate. See Table 1 on page 5 for survey summary (see Appendix C for survey results). The survey found seven instances in which agreements were canceled. Six of these occurred at the state government level and the other at the municipal level. The special circumstances and consequences of each case are highlighted below.

**Minnesota: Minnesota State Zoological Board**

The state had appropriated money to finance the acquisition and construction of a State zoological garden. The Minnesota State Zoological Board (MSZB) is not specifically authorized by law to borrow money or issue obligations in evidence. In 1977, the Legislature authorized MSZB to purchase a monorail system for the garden by installment purchase contract. The purchase price was \$8,413,000.00 payable over a 14 year period. The monorail was to be paid from receipts generated by the monorail which were deposited into the general revenue fund.

On April 1, 1980, MSZB was unable to pay an installment because revenues realized from the operation of the monorail were not sufficient. MSZB sought additional funds from the Legislature. However, the Legislature did not see the installment purchase as a state obligation. Several certificate holders sought full payment of the installment purchase through court action (United States Fire Insurance Co., et al v. MSZB).

The state district court ruled the State's only obligation under the installment agreement was to make payments thereunder from funds specifically appropriated by the Legislature for that purpose, if available. The certificate holders appealed to the State Supreme Court and on July 2, 1981, the State Supreme Court held that the state did not incur any financial obligation to certificate holders and would only incur such an obligation to the extent the Legislature appropriated funds therefor. Certificate holders' recourse was to assume operational control of the monorail, dispose of the monorail or declare the full installment purchase due, but in no event could the holders obtain judgement against the State of Minnesota.

The 1985 Minnesota Legislature authorized MSZB \$750,000.00 to settle the outstanding debt. The State's authorization was matched by \$750,000.00 in private donations. On December 30, 1985, the State acquired all investors rights to the monorail system for \$1.5 million. The documents also released the State and MSZB from all investor claims. Based on the information available, it was determined *the State of Minnesota's public bond rating was cut from AAA to A by Standard and Poor's and to AA by Moody's.*

**South Dakota:**

The State of South Dakota cancelled a lease-purchase agreement with IBM because the equipment under contract had become outdated by new technology. The case went to court and IBM prevailed. The Governor and several staff members went to New York City to lobby the rating agencies to leave the bond rating unaffected. The Executive Secretary of the South Dakota Building Authority considered limiting the December 1982 downgrade to a change from AA to AA- (Standard and Poor's) a victory of sorts. The consequences were characterized as being "significant, prompt, effective, and long lasting (10 years or more to recover with insurers)." The South Dakota state bond rating is still not back to AA despite economic growth.

**Lewisburg, Tennessee:**

The city of Lewisburg, Tennessee, failed to set aside money to pay investors for Certificates of Participation that financed a 160-acre golf course. A lawsuit was filed July 13, 1995, by First Tennessee Bank claiming city officials made "intentionally false" statements about their willingness to finance the golf course. Lewisburg did not allocate funding in the 1996 budget to fund the debt service. The two bond rating firms did not rate the issue. However, on July 17, 1995, *Moody's downgraded the city's general obligation bond to Baa1 from A.* The debt service for 1996 would have exceeded \$800,000 in an annual city budget of \$4.5 million.

**Iowa:**

The State of Iowa lease-purchased cash registers to be used in state liquor stores. The state ceased operation of the liquor stores in approximately 1986-87. The state inadvertently broke the agreement; however, the state paid its obligation in full at a later date. The rating agencies raised questions, and state officials explained the situation to the rating agencies. The Chief Financial Officer believed it would be difficult to measure the impact.

**Table 1**  
**Survey Summary**

QUESTION & NUMBER	YES RESPONSE	NO RESPONSE	N/A RESPONSE
1. Does your state permit financing by lease-purchase agreements?  Percentage of Response:	39  79.59%	10  20.41%	0  0.00%
<b>Explanation:</b> 39 states permit lease-purchase agreements and 10 do not. While 39 states provide for the use of these agreements, several states noted that they are rarely or never used.			
2. Has your state ever canceled a lease-purchase agreement?  Percentage of Response:	6  12.24%	32  65.31%	11  22.45%
<b>Explanation:</b> Officials of six states provided information about lease-purchase agreements that were terminated. The responses also yielded a lease-purchase terminated at the city level (not counted in this summary). The six states are Florida, Iowa, Minnesota, New Mexico, Oklahoma and South Dakota.			
3. If canceled, did it have an effect on your state's credit rating?  Percentage of Response:	2  4.08%	3  6.12%	44  89.80%
<b>Explanation:</b> Two of the six states had bond ratings affected. Three were cases in which it was demonstrated that a negotiable contract never existed. With regard to Iowa's case, effect is unknown and irrelevant due to the very unique circumstances of the incident.			

### **Oklahoma:**

The Oklahoma Department of Human Services (DHS) submitted a bid to the Oklahoma Office of Public Affairs (OPA) for central processing computer equipment. The bid provided a 60 month lease-purchase term with each yearly renewal conditioned on approval of the State and appropriation of funds by the Legislature. OPA accepted the bid and awarded the contract to the vendor. Subsequently, without prior approval by the OPA, DHS executed a modified agreement that included a nonsubstitution clause, which forbid termination merely to substitute other computer equipment to perform essentially the same functions. About two and a half years after the initial contract was awarded by OPA, DHS decided to upgrade its computer system and acquire new equipment rather than renew the contract. The vendor sued DHS for breach of contract. The trial court and court of appeals ruled that DHS lacked authority to agree to modified terms not accepted by OPA. The State of Oklahoma was left unharmed and bond ratings were not affected.

### **New Mexico:**

The state failed to make payments for a cogeneration facility (a facility for generating electricity) at a state penitentiary. The state did not accept the system, so no default occurred. The original purchase amount was approximately \$2,000,000 in 1986. The facility was rejected in 1989. There was litigation leading to the sale of the assets at salvage with payments to the bond holders. No effect was reflected in the state's GOB's rating. The state's bond rating was upgraded in 1993 or 1994 from AA to AA1/AA+.

### **Florida:**

A state agency entered into a lease-purchase agreement on its own accord. The State Legislature refused to meet the obligation because the agency lacked proper authority to make the agreement. The bond rating was not affected.

It is important to note the special circumstances of the cases in which ratings were either not affected, or the impact is unknown, namely the Iowa, Oklahoma, New Mexico and Florida cases. The Iowa case was somewhat of an inadvertent mistake in which the state paid the contract in full after realizing the default. Oklahoma, New Mexico and Florida were successful on the grounds that the contracts were entered into without legitimate authority to do so.

As for the other instances, the consequences seem to have been severe in each case. It is important to note that no case could be perfectly comparable to the lease-purchase agreement for the property at 601 Morris Street given the differences in financing, property under contract, state laws, and contractual differences. However, the consensus indicates cancellation of the contract would most likely precipitate a profound adverse affect on the state's bond rating.

Perhaps the most meaningful evidence provided by the survey is the fact that only two states reported ever breaking similar obligations (valid contracts) intentionally. It is clear that terminating such contracts is not a matter of common practice for the states. The PERD believes the lack of other instances is symbolic of the public perception of this option.

### **Part 3: The Secretary Of The Department Of Administration Has Had Extensive Dialog With Rating Agencies**

Our discussion with the Secretary and General Counsel of the Department of Administration corroborated the survey results (see Appendix D). In the meeting and in response to a letter from the PERD Director, the Secretary of the Department of Administration characterized the rating issue as follows:

*We believe the State is currently underrated and have been seeking an upgrade from Standard and Poor's for sometime. We also believe that Standard and Poor's is "almost" ready to grant us an upgrade. However, based on what has occurred in numerous other states and our own discussions with the rating agencies, we are very concerned that in the event we terminate the lease-purchase, we will not receive that much deserved upgrade and may possibly be downgraded.*

The Secretary went on to emphasize that he has not received a definitive answer from any of the rating agencies. According to the Secretary, it is not only State bond issues that would be subjected to the higher interest rates associated with low bond ratings and the costs of insuring bonds, but agencies and political subdivisions would have to bear the burden as well. Another area of concern for the Secretary is that canceling the lease-purchase agreement may have an impact on future lease negotiations for equipment and real property.





#### **Part 4: Analysis Of The Effects Of Canceling The Lease-Purchase Agreement**

With \$12.2 million in remaining payments as of November 1995, and an estimated property value of \$3.5 million, it is possible to view the viability of terminating the lease-purchase agreement by the application of the following model:

$$\begin{array}{l} \text{If:} \\ \text{Bond Insurance + Maintenance Liability + Other Possible Effects} < \$12.2 \text{ Million} \\ \Rightarrow \underline{\text{Terminate}}^2 \end{array}$$

**Bond insurance** is the additional capital required to insure bonds at the AAA rating level. A bond insured at AAA will require an interest rate close to equal that of a true AAA graded security. Thus bond insurance ensures the marketability of the issue as well as lowering the interest expense the state would be required to pay for a lower rated bond. The impact of a change in the State's bond rating in terms of bond insurance expenses is discussed in greater detail later in this section.

**Maintenance liability** refers to the contractual obligation of the tenant to maintain the property in a "good and tenantable condition," and that "the premises will be returned to Lessor at the termination of this lease in substantially as good condition as at the commencement thereof, normal depreciation and decay excepted." This value would also include any litigation expenses associated with a maintenance liability. Based on interviews, review of maintenance records, assessor's report, and the physical condition of the structure, we speculate that there is negligible maintenance liability if any.

**Other possible effects** includes the impact canceling the agreement may have on future credit purchases. Lease-purchase contracts for everything from buildings, such as the Diamond Department Store Building, to office equipment, such as photocopiers and large computer equipment may be affected. Given the difficulty of measuring this effect, we are only able to speculate that small lease-purchase contracts will remain unaffected because of West Virginia's history of honoring small contracts and the competitive nature of these markets. Similarly, competition will play a role in the negotiations for large contracts (building purchases and the like), but it seems obvious that the State's credit record, specifically with regard to agreements similar to that for the Morris Street Building will certainly be a factor. It is impossible to predict the effect a termination may cause in terms of unfavorable interest rates or terms for future agreements. The PERD speculates that the impact on large credit purchases will be

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<sup>2</sup> For simplicity, this model does not consider the market value of the property. It is apparent that the State would have to spend more than the market value of the building on property improvements (asbestos removal, rewiring etc.) in order to keep the building (see Appendix E). Moreover, the lack of the building's worth is shown by the fact that the Workers' Compensation Division has had to relocate its employees from the Morris Street building to an office in Kanawha City. The rent for this office is \$902,000 per year.

directly proportional to the impact the credit rating would have on WV's bonds, and the frequency of large credit purchases will be low. By this rationale, it seems likely that these costs will be substantially lower than the total cost of bond insurance.

To assess the effect of a termination on the State's bond rating, The PERD discussed the matter of bond insurance with individuals from two major bond insurance companies. These individuals provided the premium rate ranges specified in Table 2 (to be applied toward total principal and interest) upon consideration of a hypothetical bond with the following characteristics: state general obligation bond, 20 years to maturity, \$300,000,000 issue.

**Table 2**  
**Estimated Ranges for Bond Insurance**

	AMBAC	MBIA	Combined
AA	(no estimate)	18-22 basis points	(18-22 basis points)
A+	15-20 basis points	20-30 basis points	15-30 basis points
BBB+	20-25 basis points	30-40 basis points	20-40 basis points
<b>Difference Between Combined Maximum Premium Rates for AA and BBB+</b>			<b>18 basis points</b>

Because the Legislature authorized \$300 million in general obligation bonds this year to finance infrastructure projects, we have used this amount in our example. We expect any upgrade to be AA to AA- and any downgrade to be A or A-. For the purpose of demonstrating the most radical scenario and most conservative analysis possible, we are going to assume an upgrade to AA and a subsequent downgrade to BBB+. We are using 18 basis points of the total principal and interest of the bond issue as an estimate of what the State will have to pay for bond insurance to allow the BBB+ bonds to trade at the AA level (assuming 20 year maturities and AAA interest rate of 5.6%, see Appendix F. 18 basis points is the difference between the maximum premiums for the combined AA and BBB+ ranges). Bond insurance for this issue at AA would cost \$1,399,200, while at BBB+, it would cost \$2,544,000. **The difference is \$1,144,800.**

A Moody's publication entitled *An Issuer's Guide to the Rating Process* states that "evaluations are done in the context of what has taken place over the last five to ten years." Because the publication was intended for issuers of all sizes, we believe the ten year context would likely apply to the State of West Virginia on the basis that state finances are less volatile from year to year than the finances of municipalities and the like. **Our survey evidence also indicates that a change in a bond rating of a state is a lasting effect of ten years or more in duration. In the absence of a maintenance liability and other possible effects (as described in the preceding paragraphs), the State would need to issue nearly \$3.2 billion**

in bonds over the next 10-20 years to justify continuing the agreement.<sup>3</sup> At current interest and insurance rates, even a radical downgrade from AAA to BBB+ would appear to cost substantially less than the savings from canceling the lease. The net savings from canceling the lease could be over \$10 million.

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<sup>3</sup> *At 18 basis points the \$12.2 million remaining on the agreement would require \$6.8 billion in principle + interest at 5.6% interest. As interest rates increase, so to does the cost of insurance (increases are not proportional).*



## **Part 5: Maintenance Is A Responsibility Of The Tenant**

Item 4 of the lease requires "that the Tenant will maintain the leased premises, including the structure of the premises, both interior and exterior, and the electrical and plumbing fixtures and equipment in a good and tenantable condition of repair." This provision guarantees the Lessor that the property will be returned in a "good and tenantable condition of repair" should the purchase be canceled.

In addition to the maintenance, Item 8 of the contract addresses *Neglect of Premises*. It reads as follows:

*The lessee covenants that Tenant shall not commit waste on the premises herein leased, and that the premises will be returned to the Lessor at the termination of this lease in substantially as good condition as at the commencement thereof, normal depreciation and decay excepted.*

The Commissioner of Employment Programs addressed our concerns for the building's state of maintenance in a recent interview. He explained that the building is in better condition now than at the commencement of the lease. Many improvements have been made to the building such as the new ventilation system, repairs to badly decayed structures, and fire safety improvements. An appraiser's report and a Legislative Auditor's Report indicate problems with the building have existed since before commencement of the lease and soon thereafter, respectively.

While gains from terminating the lease could be partially offset by the expense of restoring the building, the PERD believes the State has no maintenance liability for the property. In the case that there would be a maintenance liability, any action against the state would have to go through the State Court of Claims. In addition, any monetary awards by the Court of Claims would then be required to be approved by the Legislature.



## **Part 6: Other Options Should Be Considered**

The PERD believes the state could possibly negotiate a cancellation of the lease. By settling, the state may be able to still see its financial rating upgraded and achieve most of the cost savings from an out-right lease cancellation. Third parties may have interests in the facility or location and may be willing to assume a portion of the contract. A settlement could possibly earn a vote of confidence from the raters. However, it may be necessary for the Legislature to provide authority to the Secretary of the Department of Administration to make a settlement.

If negotiations are unsuccessful, and the state chooses not to cancel the lease and becomes stuck with the building, the state should consider using/modifying the building for other purposes, i.e. the storage of records or other property, or if the state would renovate the building, placing a state agency back in the Morris Street building. The PERD is not prepared to make specific alternative use recommendations at this time.





## **Part 7: Conclusion And Recommendations**

The building lease and state law clearly allow for the cancellation of the lease-purchase agreement. However, based upon its nationwide survey, discussions with financial officers in other states and discussions with a nationally recognized financial expert, the PERD believes that canceling the lease on the Morris Street building would negatively affect the state's bond rating. **Thus, as previously stated, PERD, believes that a negotiated cancellation of the agreement is the best option.** By settling, the state may be able to still see its financial rating upgraded and achieve most of the cost savings from an outright lease cancellation.

**However, if a negotiated settlement is not quickly reached, part 13 of the lease-purchase agreement should be invoked by the state canceling the agreement.** Although this action might result in the state's credit rating not being upgraded to AA from its present A+, the benefit from canceling the lease is greater than the cost of a lower financial rating. **Even in the worst case scenario of the state's financial rating being downgraded to a BBB+ as opposed to receiving an upgrade to AA, it would require the state issuing almost \$3.2 billion in additional bonds before the cost of additional bond insurance would equal the \$12.2 million the state would save from canceling the Morris Street Building lease-purchase.**

### **Recommendation 1**

*The Secretary of Administration should continue to attempt to reach a negotiated cancellation of the lease-purchase agreement for the Morris Street building.*

### **Recommendation 2**

*If the Secretary of Administration is unable to reach a negotiated settlement with the owners of the Morris Street building within 30 days, the Secretary of Administration should invoke part 13 of the agreement and give 30 days notice that he is canceling the lease-purchase of the building. The Secretary should report his actions concerning this matter to the Joint Committee on Government Operations by December 1995.*

Furthermore, although the Morris Street Building clearly was not worth the \$19 million the previous administration agreed to pay for it, and the lease contains a legally valid cancellation clause, the financial markets expect the State of West Virginia to treat the lease as if it was a general obligation bond backed by the full faith and credit of the state. Therefore, although legally the lease-purchase's termination provisions did not bind future Legislatures to agreements made by the previous administration, in actuality it has. **In fact, based upon its analysis, the PERD finds that all lease-purchase agreements which are legally entered into by any gubernatorial administration, in the opinion of the financial raters, binds future Legislatures to honor the agreements until they are paid in full.**

### **Recommendation 3**

*The Legislature should consider amending state law to require direct Legislative approval of all long-term and large sum lease-purchase agreements. The amount and terms of an agreement which would require legislative approval should be clearly stated if the Legislature chooses to amend state law.*

## **Appendix A**

### **Research Objective and Methodology**

As a part of the performance audit of the Workers' Compensation Division, the PERD conducted research to determine the contract options and their consequences regarding the lease-purchase agreement for the property at 601 Morris Street, Charleston. Particular emphasis has been given to determining the consequences of terminating the lease-purchase agreement.

The methodology included a survey of financial officers of the 49 states, discussions with attorneys, interview of the Secretary of Administration, discussion with a nationally recognized expert on government finance, analysis of the lease-purchase contract, analysis of the infrastructure bill (H.B. 2037) passed in the 1995 Legislative Session, review of newspaper articles, and a cost-benefit analysis based on available information. The PERD abstained from dialog with the rating agencies for the fear that "street talk" could jeopardize the state's bond rating.



## **Appendix B**

### **Lease-Purchase Survey**

1. Does your state permit the financing of government buildings through lease-purchase agreements?
  
2. If your state has financed buildings through lease-purchase agreements, has your state ever canceled a lease-purchase agreement? If possible, please provide details of the canceled agreement, including the original lease-purchase amount, the number of years the agreement was for, the year in which the agreement was canceled (i.e., the second, third, etc. year of the contract), and whether your state was sued by the bondholders or the company which insured the lease-purchase bonds.
  
3. If your state has canceled lease-purchase agreements for the financing of capital projects, did the cancellation have a negative impact on your state's credit rating by either Standard and Poor's or Moody's financial services? If possible, please provide details as to your state's bond rating prior to the cancellation of the lease-purchase agreement and the bond rating six months after the cancellation.
  
4. If we have additional questions concerning your state's cancellation of lease-purchase agreements, who should we contact for additional information? Please provide their phone number.









# Appendix D

## Correspondence from Secretary of Department of Administration



STATE OF WEST VIRGINIA  
DEPARTMENT OF ADMINISTRATION  
State Capitol  
Charleston, WV 25305

RECEIVED

SEP 12 1995

RESEARCH AND PERFORMANCE  
EVALUATION DIVISION

Gaston Caperton  
Governor

Chuck Polan  
Cabinet Secretary

September 11, 1995

Antonio E. Jones, Ph. D.  
Director  
Performance Evaluation and Research Division  
West Virginia Legislature  
Building 5, Room 751A  
1900 Kanawha Boulevard, East  
Charleston, West Virginia 25305-0592

Dear Dr. Jones:

In response to your letter of September 8, 1995 and our meeting that day, we have discussed the issue of terminating the lease-purchase agreement for the facility located at 601 Morris Street in Charleston with Standard & Poor's, as well as the other two rating agencies. Based on those discussions, we are unsure exactly what effect the termination would have on the credit rating of the State.

We believe the State is currently underrated and have been seeking an upgrade from Standard & Poor's for sometime. We also believe that Standard & Poor's is "almost" ready to grant us an upgrade. However, based on what has occurred in numerous other states and our own discussions with the rating agencies, we are very concerned that in the event we terminate the lease-purchase, we will not receive that much deserved upgrade and may possibly be down graded. The specific question of what impact terminating the lease-purchase agreement will have on our credit rating has been posed to the rating agencies on numerous occasions, but we have not received a definitive answer.

In reality, the effect on the credit rating is only one of various factors that must be considered. Other matters, such as paying for a building that offers the State nothing but a reminder of how not to do business and future leasing of equipment and real property, must be considered. The problem is that there is no easy answer.

You have also inquired as to my assessment of the interest differential between the various ratings. Each day the market changes and the response will change accordingly. Based on information we have been provided for the current market, it appears that if the State is upgraded by Standard & Poor's to a AA

E.E.O./AFFIRMATIVE ACTION EMPLOYER


**DEPARTMENT OF ADMINISTRATION**

Antonio E. Jones, Ph. D.  
September 11, 1995  
Page two

we could save between five and fifteen basis points in interest on each issue over our current rating of A+, depending on the nature of the issue. If the State is downgraded to an A, the cost is even more, being at least seven to twenty basis points on each issue. If the downgrade were more severe, the cost would be even higher. In addition to the State, each of the State agencies issuing bonds will be impacted, as well as the political subdivisions.

If you wish to discuss this matter further, do not hesitate to contact me or Diana Stout. We appreciate the time you and your staff spent with us on Friday.

Sincerely,



Chuck Polan  
Secretary

CP/tj

## Appendix E

### Correspondence from Commissioner of Bureau of Employment Programs

**Bureau of Employment Programs**  
112 California Avenue  
Charleston, West Virginia 25305-0112

Gaston Caperton  
Governor  
Andrew N. Richardson  
Commissioner



October 6, 1995

Mr. Antonio E. Jones  
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1900 Kanawha Boulevard, East  
Charleston, West Virginia 25305-0592

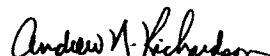
Dear Mr. Jones:

In response to your letter dated September 26, 1995, I am submitting to you a copy of a report sent to the Secretary of CLER on July 27, 1993. The report is comprehensive, as it covers all aspects of the work required to bring the facility into compliance with Fire and Safety Regulations, as well as the Americans with Disabilities Act requirements.

Since that report was submitted, two additional areas of concern were brought to my attention that escalated final costs. Attached is a copy of a letter sent by the architects which projected additional electrical work requiring revision of previous estimate of \$369,000 to \$2,448,600. Later asbestos was discovered in an area of the building where we were planning to put our new claims teams. See attached letter for cost breakdown concerning the removal of the asbestos, totaling \$78,849.

As the tenant, not the lessee, I have no future plans for the facility. The Bureau of Employment Programs will have no need for the facility after all remaining employees are moved to a safe, habitable work environment. I do not know what plans the Department of Administration may have for the facility.

Sincerely,

  
Andrew N. Richardson  
Commissioner

Attachments

	SCHEME 1	SCHEME 2	SCHEME 3
<u>SPRINKLER SYSTEM</u> 130,420 SF @ \$ 1.50/SF	\$ 195,630.00	\$ 195,630.00	\$ 195,630.00
<u>FIRE ALARM SYSTEM</u> 130,420 SF @ \$ 0.50/SF	65,210.00	65,210.00	65,210.00
<u>ELECTRIC RE-WIRING/LIGHTING</u> 130,240 SF @ \$ 7.00/SF	912,940.00	912,940.00	912,940.00
<u>EMERGENCY GENERATOR</u> Allowance	150,000.00	150,000.00	150,000.00
<u>INDEPENDENT SMOKE CONTROL</u> 130,240 SF @ \$ 2.00/SF	260,840.00		
<u>HVAC/INTEGRATED SMOKE CONTROL</u> 130,420 SF @ \$ 8.00/SF			870,720.00
<u>INDEPENDENT SMOKE CONTROL/VENTILATION</u> 130,420 SF @ \$ 2.00/SF SMOKE CONTROL 92,200 SF @ \$ 6.00/SF VENTILATION 1-4		260,840.00 553,200.00	
<u>HVAC/SMOKE CONTROL - CONTROLS</u> 130,420 SF @ \$ 1.00/SF		130,420.00	130,420.00
<u>ELEVATOR UP-GRADE</u> Upgrade 2 Existing Elevators 12 Stops @ \$2,000.00/Stop Add 2 Elevators/5 Stops 10 Stops @ \$20,000.00/Stop Up-Grade Existing 7-Stop Elev. 7 Stops @ \$2,000.00/Stop Add 2 Elevator/7 Stops 14 Stops @ \$20,000.00/Stop Enclosure 3,600 SF @ \$15.00/SF 5,500 SF @ \$15.00/SF	24,000.00	200,000.00 14,000.00 54,000.00	280,000.00 82,500.00
<u>HANDICAPPED ACCESSIBILITY (TOILETS)</u> 7 Floors \$ 5,000.00/EA	35,000.00	35,000.00	35,000.00
<u>DEMOLITION</u> 130,420 SF @ \$ 2.00/SF	260,840.00	260,840.00	260,840.00
<u>NEW CONSTRUCTION</u> 130,420 SF @ \$10.00/SF	1,304,200.00	1,304,200.00	1,304,200.00
<u>REMOVAL OF HAZARDOUS MATERIALS</u> 36,036 SF @ \$ 5.00/SF	180,180.00	180,180.00	180,180.00
<u>FAÇADE UP-GRADE</u> 40,000 SF @ \$ 15.00/SF			600,000.00
<u>NEW STAIRWAYS</u> 384 Risers @ \$ 200.00/Riser Enclosure: 1,800 SF @ \$ 6.00/SF 2,700 SF @ \$10.00/SF 8,500 SF @ \$10.00/SF	76,800.00 10,800.00 27,000.00	76,800.00 85,000.00	76,800.00 85,000.00
<u>MECHANICAL ROOM/ENTRANCE ADDITIONS</u> 1,800 SF @ \$ 60.00/SF		108,000.00	108,000.00
TOTAL	3,503,440.00	4,053,220.00	5,337,440.00
GCOH&P @ 30%	1,051,030.00	1,215,970.00	1,601,230.00
CONSTRUCTION COST	4,104,470.00	5,269,190.00	6,938,670.00
CONTINGENCY @ 15%	615,670.00	790,380.00	1,040,800.00
TOTAL	4,720,140.00	6,059,570.00	7,979,470.00

STATE OF WEST VIRGINIA  
DEPARTMENT OF PUBLIC SAFETY  
STATE FIRE MARSHAL'S OFFICE

Capitol Complex  
Charleston, West Virginia 25305

(304) 558-2191  
FAX: (304) 558-2537

FIRE SAFETY INSPECTION REPORT

West Virginia					
<u>Workers Compensation Building</u>		<u>June 28, 1993</u>		<u>558-0476</u>	
Name of Facility (Complex)		Date of Inspection		Telephone Number	
<u>Business</u>		<u>Dave Clark, Director</u>			
Building		Executive Officer - Title			
Occupancy Type		Address			
<u>601 Morris St.</u>		<u>Charleston</u>		<u>Kanawha WV 25301</u>	
Address - Street		City		County State Zip Code	
<u>Type I 332</u>		<u>6 story</u>		<u>130,631</u>	
Construction Type		Height		Square Footage Occupant Load	
<u>R. Raynes/Walter Snyder</u>				<u>Fire Alarm Yes</u>	
Inspector/accompanied by:				<u>Sprinkler No</u>	
				<u>Fire Drills</u>	

REQUIREMENTS

Previous Inspection January 17, 1991.

The overall evaluation of this building for fire safety is very serious. Immediate action is imperative to correct the serious life safety problems or the building should be vacated.

1. This building does not have exits that meet fire code requirements. Provide approved exiting from every floor. (Exits are not remote from each other, non-uniform tread/riser dimensions, stair dimension exceeds allowable standards, door swing at several locations reduces stair landing by more than one-half, there shall be no usable space within an exit enclosure).  
NFPA 101 27-2.4 (1/91)
2. An approved electrically supervised fire alarm system shall be installed throughout the building in accordance with Section 11 of the State Fire Code. This includes but is not limited to smoke detectors in ducts of required HVAC equipment to permit automatic shutdown, additional audio-visual alarm signals and thermal detectors in hazardous areas.  
SFC Section 11 (1/91)
3. All vertical openings throughout the building shall be 2 hour fire-rated construction. (Unprotected openings in stairways, floor openings for the passage of pipe penetrations in janitor closets and electrical rooms).  
NFPA 101 27-3.1.1 (1/91)

REQUIREMENTS LISTED ARE NOTIFICATION OF FIRE CODE VIOLATIONS

NFPA - National Fire Protection Association SFC - State Fire Code

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EMPLOYMENT PROGRAMS  
JUL 27 1993  
FAM Admin

West Virginia  
Workers Comp. Building  
Page Two

4. Separate all hazardous areas throughout the building-(storage rooms, janitor closets, mechanical rooms, kitchen) with one hour fire-rated construction, including 3/4 hour fire-rated door assembly.  
NFPA 101 27-3.2.1 (1/91)
5. Upgrade electrical wiring to meet National Electric Code. (Steel pull and junction boxes above ceiling not supported, conduit not securely fastened in place every 10 feet and within 3 feet of each outlet box, unlabeled distribution panels, unused openings in distribution panels, BX cable not secured, splices not in junction box, etc.)  
NFPA 70 (1/91)
6. Ceiling cavity plenum on every floor shall not contain any combustible material, fire stopping is not maintained, light diffusers are not listed, etc. (Unprotected electrical wiring and numerous cables noted).  
NFPA 90A (1/91)
7. Foam type insulation sprayed-on ceiling of top floors and elevator penthouse does not meet code requirements. This foam is highly combustible and is not protected from thermal or ignition sources.  
NFPA 90A 2-3.10 (1/91)
8. No dead-end corridor shall exceed 50 feet. Several corridors exceed this requirement.  
NFPA 101 27-2.5.2 (1/91)
9. Additional exit and directional signs are needed throughout the building. Disorientation is obvious due to a lack of these signs.  
NFPA 101 27-2.10 (1/91)
10. All corridors throughout the building shall be maintained free and clear of storage at all times.  
NFPA 101 31-1.2.1 (1/91)
11. Several emergency lights and exit signs are not working.  
NFPA 101 31-1.3.1 (1/91)
12. Several areas of the building contain polystyrene foam panels on inside walls. These panels do not meet interior finish requirements. It is also used to cutoff vertical openings, which is not permitted.  
NFPA 101 27-3.3 (1/91)
13. Ammonia hydroxide storage located in the basement is not properly fire separated. Proper ventilation is also required for this material when used in employee working environment.  
NFPA 101 27-3.2.1 (1/91)
14. Provide specifications for carpet on walls and columns to meet interior finish requirements.  
NFPA 101 27-3.3 (1/91)

West Virginia  
Workers Comp. Building  
Page Three

15. Where carpet passes under fire-rated doors a noncombustible strip is required.  
NFPA 80 (1/91)
16. PVC sewer vent pipe installed in spiral stairway is not permitted.  
NFPA 27-3.3 (1/91)
17. Elevators do not meet ANSI A17.1 requirements.  
NFPA 101 7-4.2 (1/91)

NOTE: It is highly recommended that a complete automatic sprinkler system be installed throughout the building in accordance with NFPA 13 because many areas with offices do not have windows.

NOTE: Renovations on Governor's desk for approval. Each floor will be gutted and rebuilt with 3 stair towers.

Fire Ext. 11/92

Orig: Director  
cc: Joint Committee on Government Organization, The Honorable  
Jae Spears, State Senator, Room 223 West Wing, State Capitol  
cc: Secretary Charles Polan  
State Board of Risk Management  
Commissioner Andrew Richardson  
Inspector  
File

07/16/93  
dh



July 29, 1994



Mr. Randall L. Bare  
Bureau of Employment Programs  
State of West Virginia  
4401 MacCorkle Avenue, SE  
Charleston, WV 25304

Re: Workers' Compensation Fund Building Electrical Upgrade  
601 Morris Street

Dear Mr. Bare:

As per your request, you will find enclosed a Preliminary Cost Estimate for upgrading your current electrical system to allow for the installation of a new computer system which will be installed throughout the entire 130,000 SF building located at 601 Morris Street.

Without going through an extensive cost estimate, at this time, it is our best judgement that the total cost to do this work should not exceed \$2,448,600. This price would allow for a new electrical service entrance, complete re-wiring of the existing building, removal of the existing ceilings as needed and the replacement of those ceilings after the work is completed.

As always, if you have any questions please do not hesitate to call.

Sincerely,

ZMM, INC.

A handwritten signature in dark ink, appearing to read "Michael E. Henley", is written over a horizontal line.

Michael E. Henley, AIA

 ZMM, INC.  
ARCHITECTS • ENGINEERS

222 LEE STREET W. • CHARLESTON, WEST VIRGINIA 25302  
(304) 342-0159 • FAX (304) 345-8144

Workers' Compensation Fund Building Electrical Upgrade, 601 Morris Street  
Preliminary Cost Estimate  
July 29, 1994

1.	New Electrical Service - Lump Sum	=	\$ 200,000
2.	Re-wiring of existing Building - 130,000 SF @ \$8.00	=	1,040,000
3.	Removal of existing ceilings - 130,000 SF @ \$1.50	=	195,000
4.	New ceilings - 130,000 SF @ \$2.50	=	<u>325,000</u>
	Subtotal		\$1,760,000
	Profit and Overhead @ 25%	=	440,000
	Contingency @ 5%	=	<u>110,000</u>
	Total		\$2,310,000
	Architectural Fee @ 6%		\$ 138,600
	Total		<u>\$2,448,600</u>

*Charleston*

Bureau of Employment Programs  
**Workers' Compensation Division**  
601 Morris Street  
Charleston, West Virginia 25301-1446

Gaston Caperton, Governor  
John Ranson, Cabinet Secretary,  
Commerce, Labor and Environmental Resources  
Andrew N. Richardson, Commissioner,  
Employment Programs



M E M O R A N D U M

TO: Ed Burdette  
FROM: Dave Thomas *DT*  
DATE: April 28, 1994  
RE: Cost of Asbestos Discovery

*CC*  
*for Randy Base*  
*4/30/94*  
*Thomas*

The presence of asbestos recently discovered in the WCD building is estimated to cost the WCD \$78,849 for inspection, sampling, and removal of asbestos, for relocation of 15 employees, and for lost productivity of those employees.

As of April 28, 1994, actual costs incurred are \$18,787, projected costs are \$58,530, and estimated costs are \$1,532.

Attached is an itemization of actual, projected, and estimated costs. A more detailed itemization is available.

cc: Ed Staats  
Lisa Jackson

WCF 10/1/94

2 MAY 04 11: 03

*An Equal Opportunity/Affirmative Action Employer*

Itemized Costs of Asbestos Situation

Lost-productivity estimates of salaries take into account the time necessary to move relocated personnel back to the asbestos-affected area.

	<u>Cost</u>
One-day's salary of 12 permanent WCD employees who were relocated, plus WCD's associated FICA and PERS costs (7.65% and 9.5%, respectively) (Estimated)	\$ 1,056
One-day's salary of three Olsten temporaries who were relocated (Estimated)	96
Garland Jarrell's overtime salary, plus FICA and PERS costs (Actual)	144
One-day's salary for Garland Jarrell for moving employees, plus FICA and PERS costs (Estimated)	105
One-day's salary for Ronnie Hodges for moving employees, plus FICA and PERS costs (Estimated)	158
Cost of two Work Release workers for assisting Garland during his overtime hours (Actual)	27
Cost of two Work Release workers for moving employees (Estimated)	117
Asbestos inspection by Astech (Actual)	5,600
Air sampling by Astech (Actual)	12,666
Relocation of telephone service (Actual)	350
Proposal by Astech for removal of asbestos and cleanup (Projected)	<u>58,530</u>
Total	\$78,849



**Appendix F**  
**Approximations of Municipal Bond Yields by Grade and Maturity**  
**September 20, 1995**

<b>Maturity</b>	<b>AAA</b>	<b>AA</b>	<b>A-1</b>	<b>A</b>	<b>BAA-1</b>
1 year	3.70	3.80	3.90	4.00	4.20
2 years	3.85	3.95	4.05	4.15	4.35
3 years	3.95	4.05	4.15	4.25	4.45
4 years	4.10	4.20	4.30	4.40	4.60
5 years	4.20	4.30	4.40	4.50	4.70
6 years	4.35	4.45	4.55	4.65	4.75
7 years	4.45	4.55	4.65	4.75	4.95
8 years	4.55	4.65	4.75	4.85	5.05
9 years	4.65	4.75	4.85	4.95	5.15
10 years	4.75	4.85	4.95	5.05	5.25
11 years	4.90	5.00	5.10	5.20	5.40
12 years	5.00	5.10	5.20	5.30	5.50
13 years	5.10	5.20	5.30	5.40	5.60
14 years	5.20	5.30	5.40	5.50	5.70
15 years	5.30	5.40	5.50	5.60	5.80
16 years	5.40	5.50	5.60	5.70	5.90
17 years	5.50	5.60	5.70	5.80	6.00
18 years	5.55	5.65	5.75	5.85	6.05
19 years	5.60	5.70	5.80	5.90	6.10
20 years	5.60	5.70	5.80	5.90	6.10
25 years	5.65	5.75	5.85	5.95	6.15
30 years	5.70	5.80	5.90	6.00	6.20

Source: MMS International  
Note: Municipal bond yields are a good proxy for state general obligation yields. State bond yields are slightly lower, but differences are proportional.

