House Revenue Committee

Overview of the 2015 State Debt Policy Advisory Commission Report

Office of the State Treasurer
Debt Management Division

February 10, 2015

Introduction

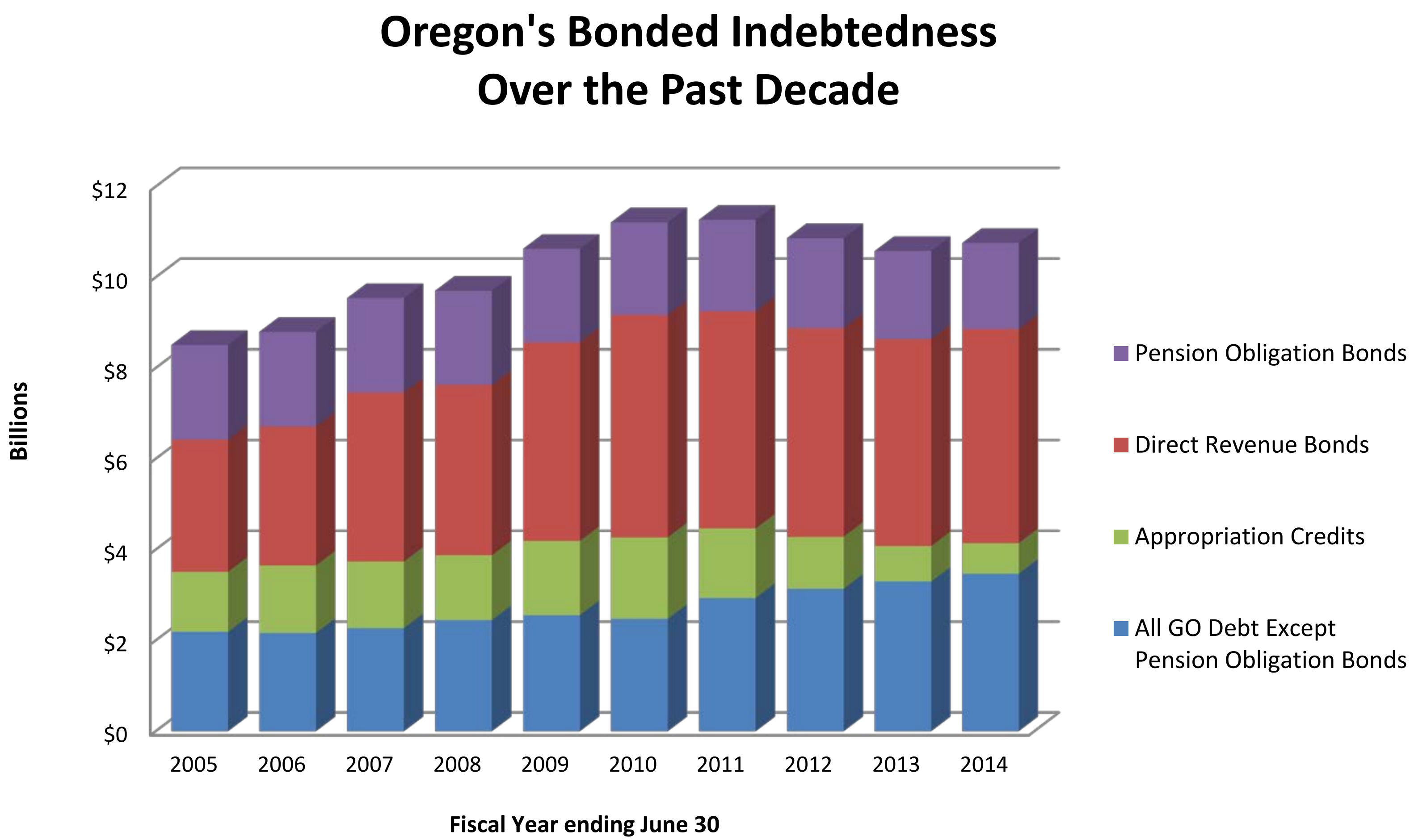
Purposes of Report

1. Annual Capacity Forecast Update Required by ORS 286A.255
2. Provide a Framework for Measuring, Monitoring and Managing the State's Debt Position
3. Provide Information to Assist Governor and Legislature in Formulating Long-term Capital Spending Plans
4. Highlight Emerging Debt Policy Issues of Concern

Debt Capacity Concepts

Four Types of Long-Term Debt

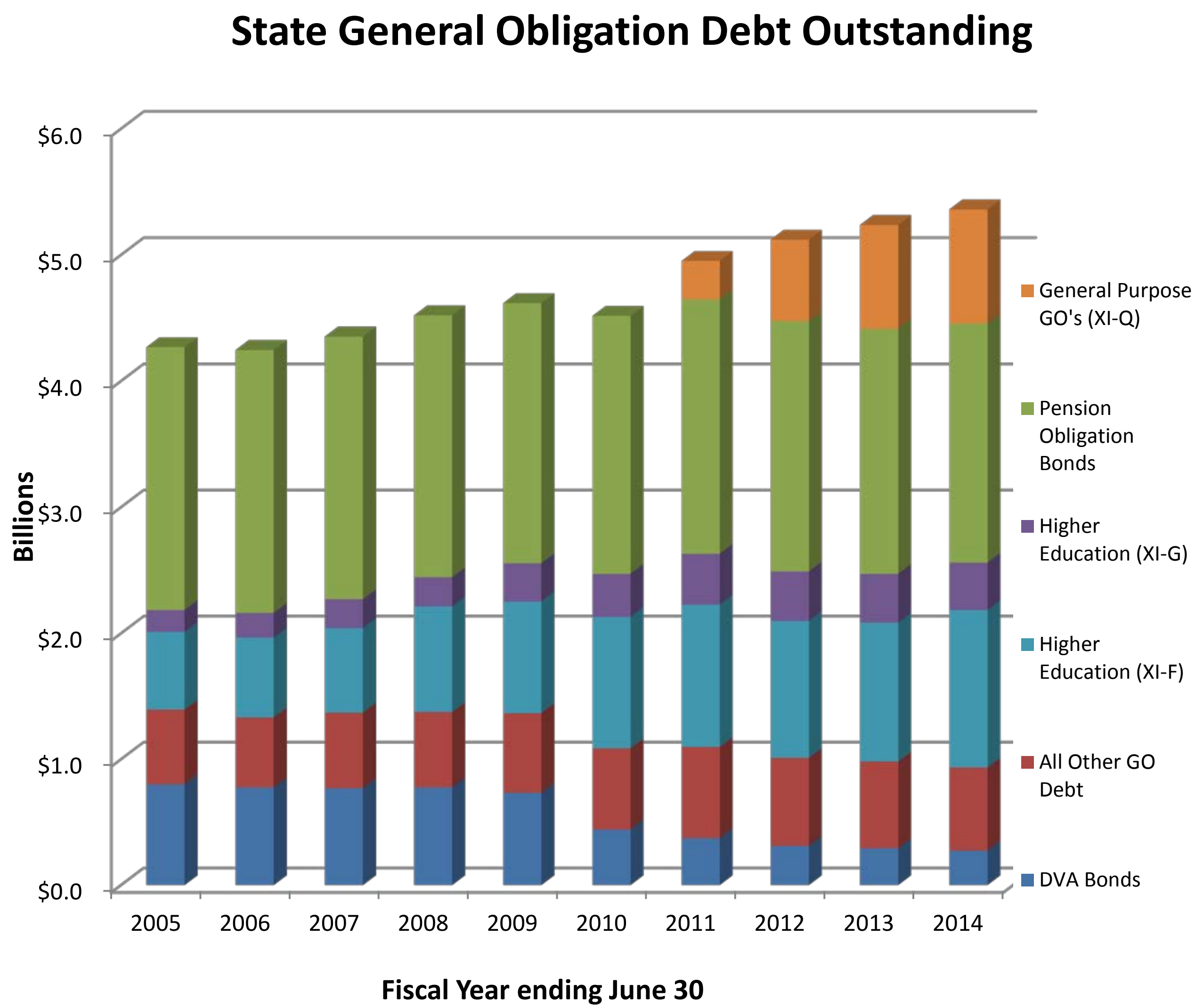
1. General Obligation Bonds	• Requires voter approved constitutional amendment • Pledges the full faith & credit of the State • Includes both GF-supported and non GF-supported bond programs
2. Direct Revenue Bonds	• Generally created by the Legislature through statute • Not secured by the State's pledge to pay • Fully self-supporting through program revenues
3. Appropriation Credits	• Historically, Certificates of Participation (COPs) were used to finance real or personal property owned by the State • Generally payable by State agencies from GF sources • Not secured by the full faith and credit of the State • With passage of XI-Q GO bond authorization in 2010, higher cost COPs are not often used for State capital projects
4. Conduit Revenue Bonds	• State is the issuer but has no obligation to pay debt service – no General Fund or other State support • Debt service paid by the entities on whose behalf the bonds are issued



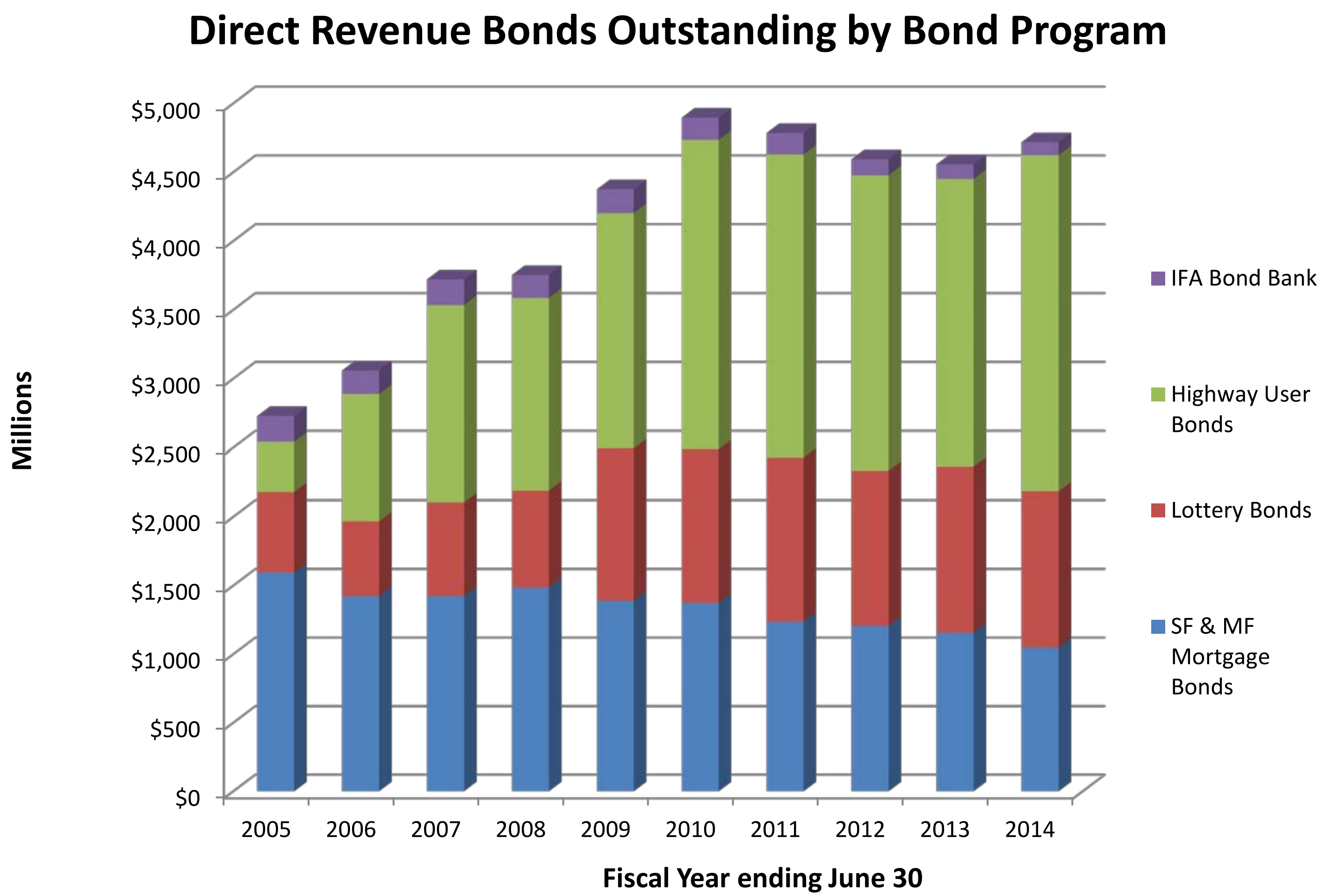
- The State's overall debt levels rose steadily from FY 2005 through FY 2010, but has remained relatively stable since then, as existing debt retirement has generally kept pace with new debt issuance

Debt Capacity Concepts

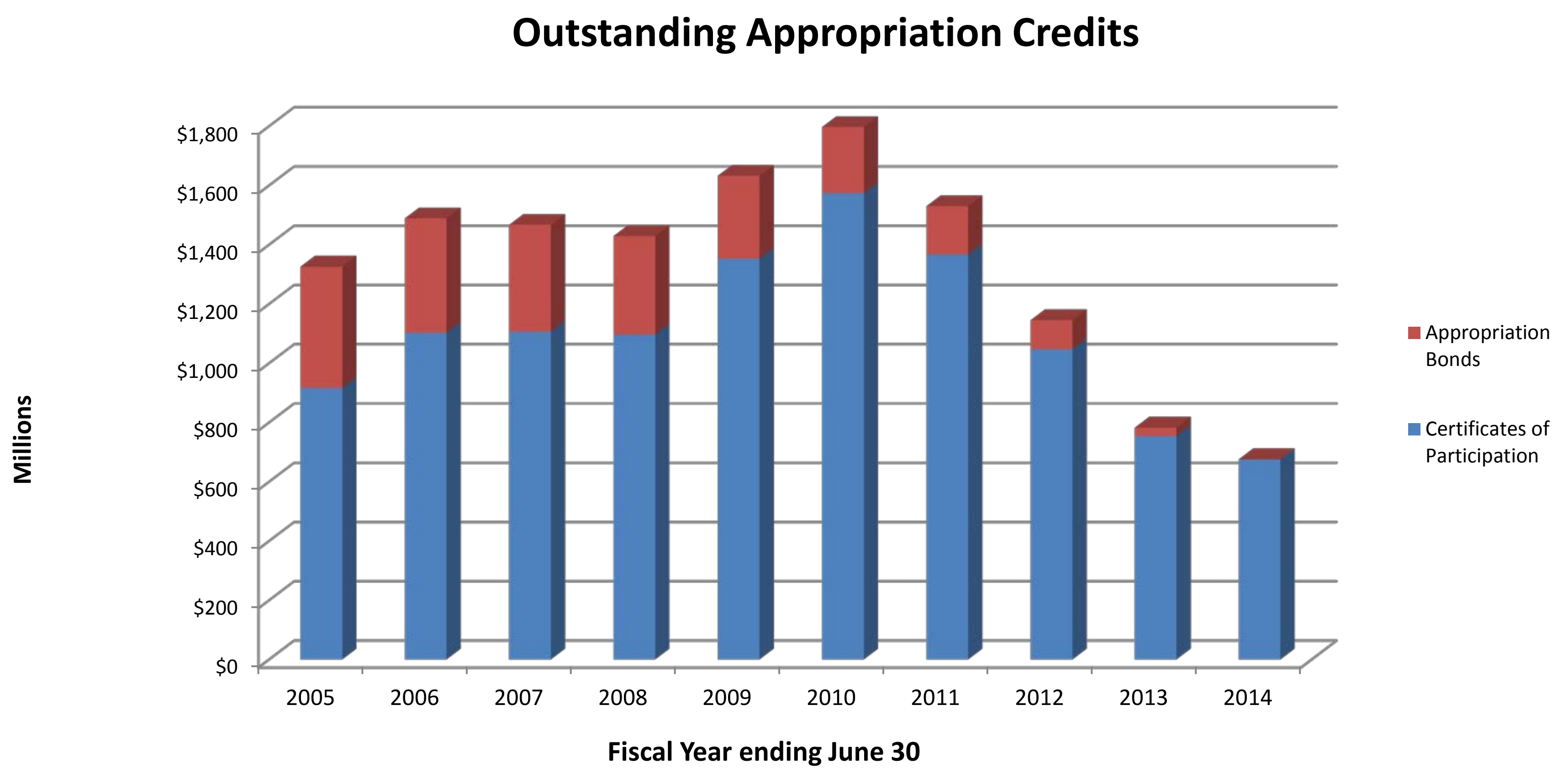
- In FY 2004, the State issued $2.4 billion in Pension Obligation Bonds, of which $1.9 billion remained outstanding at the end of FY 2014
- In recent years, most new GO bonds were issued to fund building projects at public universities and community colleges
  - $1.9 billion of this type of debt was outstanding as of June 30, 2014
- Since FY 2011, the State has issued $472 million in XI-Q bonds to refund existing COPs, saving $57 million in interest costs over the life of these bonds



Debt Capacity Concepts



- The issuance of $2.8 billion in Highway User Tax Bonds to fund ODOT's multi-year bridge and highway improvement and congestion management programs is responsible for the majority of the growth in outstanding state revenue bonds
- With the introduction of video line games in 2005, both net Lottery revenues and Lottery debt issuance increased substantially over the last ten years



- The final payment on the appropriation deficit bonds sold in 2003 was made in September 2013
- The State continues to refund existing COPs with lower cost Article XI-Q GO bonds whenever financially feasible, saving an estimated $57.1 million in interest costs to date

Four Debt Capacity Categories

1. General Fund-Supported Debt	• SDPAC Recommended Target Limit -- 5% of General Fund Revenues
2. Lottery-Backed Debt	• Legal Bond Covenant Limit: 4x Coverage (no more than 25% of net lottery revenues) • Moral obligation pledge of State
3. Net Tax-Supported Debt	• National bond rating agency perspective. • States compared with each other using "apples-to-apples" measurement approach
4. Non Tax-Supported Debt	• No generic capacity limit or measurement. • State programs in this category are managed based on revenue streams available

General Fund-Supported Debt Programs

GF-Supported State Debt Programs

General Obligation Bonds

- Higher Education Facility Bonds (XI-G)
- Community College Bonds (XI-G)
- Pollution Control Bonds (42% of total)
- Alternate Energy Bonds (33% of total)
- Oregon Opportunity Bonds (OHSU)
- Pension Obligation Bonds (32% of total)
- Seismic Rehabilitation Public Education Buildings (XI-M)
- Seismic Rehabilitation Emergency Service Buildings (XI-N)
- State General Purpose (XI-Q) (85% of total)

Appropriation Credits

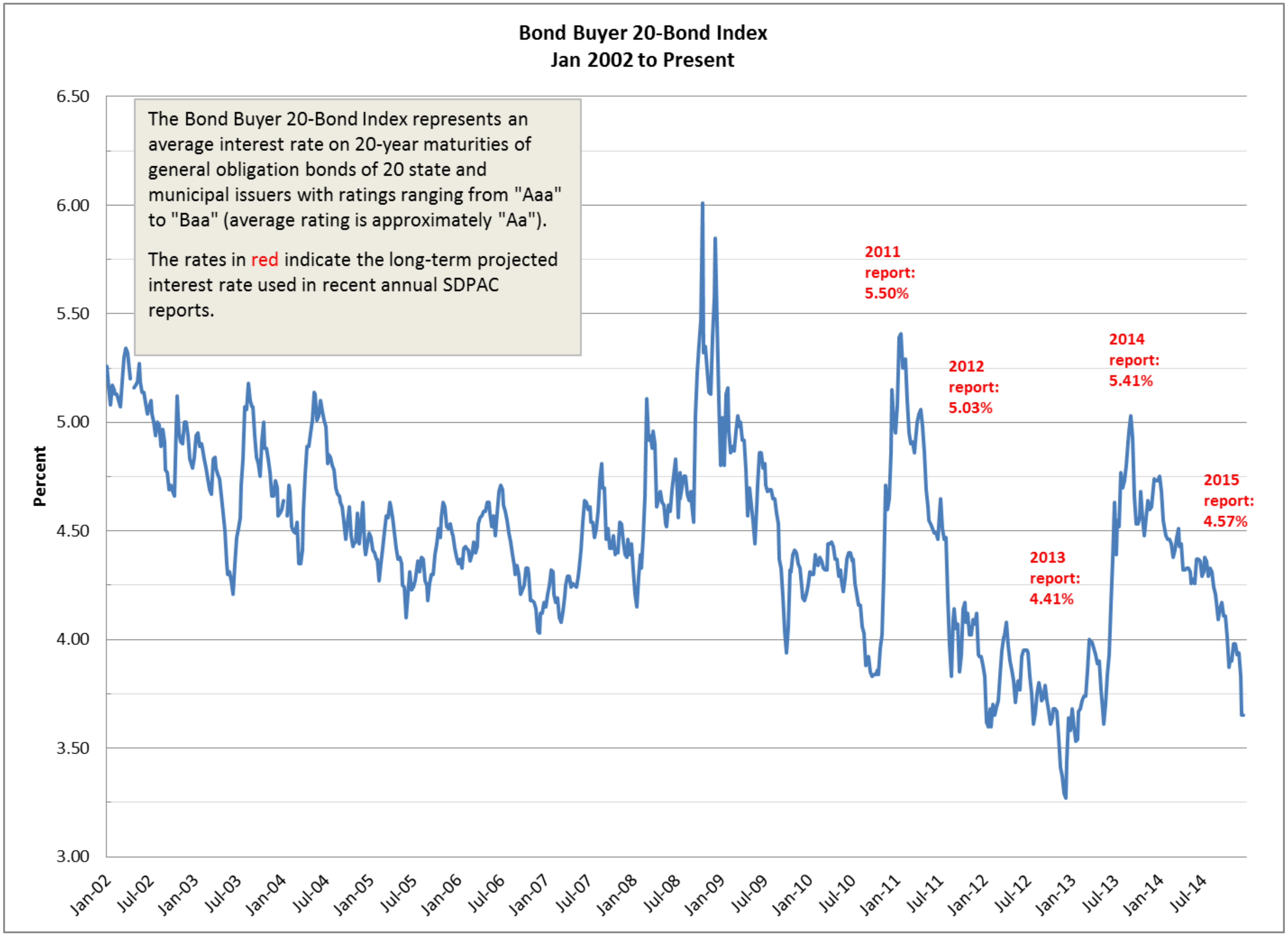
- Certificates of Participation (85% of total)

Outstanding as of June 30, 2014 -- $2.7 Billion

Model Inputs & Assumptions

- Accounts for all debt outstanding as of June 30, 2014 and assumes **$843.5 million** in planned issuance during the current biennium based on 2013 and 2014 legislative authorizations for General Fund-supported GO bonds, including:
  - *$400.8 M for State Buildings (XI-Q) (General Fund-supported only)*
  - *$402.6 M for Higher Education Facilities , OHSU ‘s Cancer Research Center, and Community College projects (XI-G)*
  - *$30 M for school and public safety building seismic upgrade grants (XI-M & XI-N)*
  - *$10 M for environmental quality projects (XI-H)*
- Uses December 2014 General Fund revenue forecast over eight year horizon
- New debt issued as level debt service over 20 year term at **4.87%** interest rate (average BB-20 over last 10 years plus 50 bps)
- Target of 5.0% of General Fund revenues used to make payment on General Fund debt service

General Fund-Supported Debt



Projected General Fund-Supported Debt Capacity
over the Next Eight Years

Fiscal Year Ending June 30	Maximum Amount that can be Issued within Target Capacity ($ Millions)	Debt Service as a % of General Fund Revenues
2015	--	3.5%
2016	1,177	5.0%
2017	358	5.0%
2018	319	5.0%
2019	424	5.0%
2020	323	5.0%
2021	409	5.0%
2022	531	5.0%
2023	353	5.0%
Additional General Fund Capacity Over the Forecast Period	**$ 3,896**	

*These amounts do not Include the $843.5 million in GF-supported bonds authorized by the 2013 and 2014 Legislatures

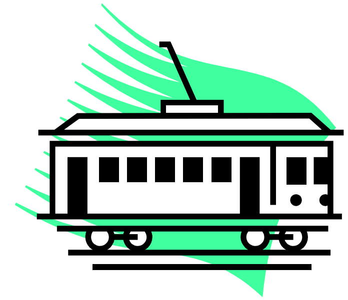
Factors that Could Impact Projected General Fund Debt Capacity

	FY 2016 – FY 2023*	Per Biennium **
Base Case	**$ 3,896**	**$ 974**
Change in General Fund forecast		
10% decline	3,139	784
10% increase	4,652	1,163
Change in interest rate forecast		
1.0% higher	3,584	896
1.0% lower	4,251	1,063

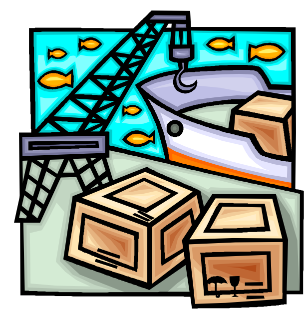
* Does not include the $843.5 million in GF supported bonds authorized by the 2013 and 2014 Legislatures
** May not total exactly due to rounding

Lottery-Backed Debt

Lottery Bond Projects & Programs



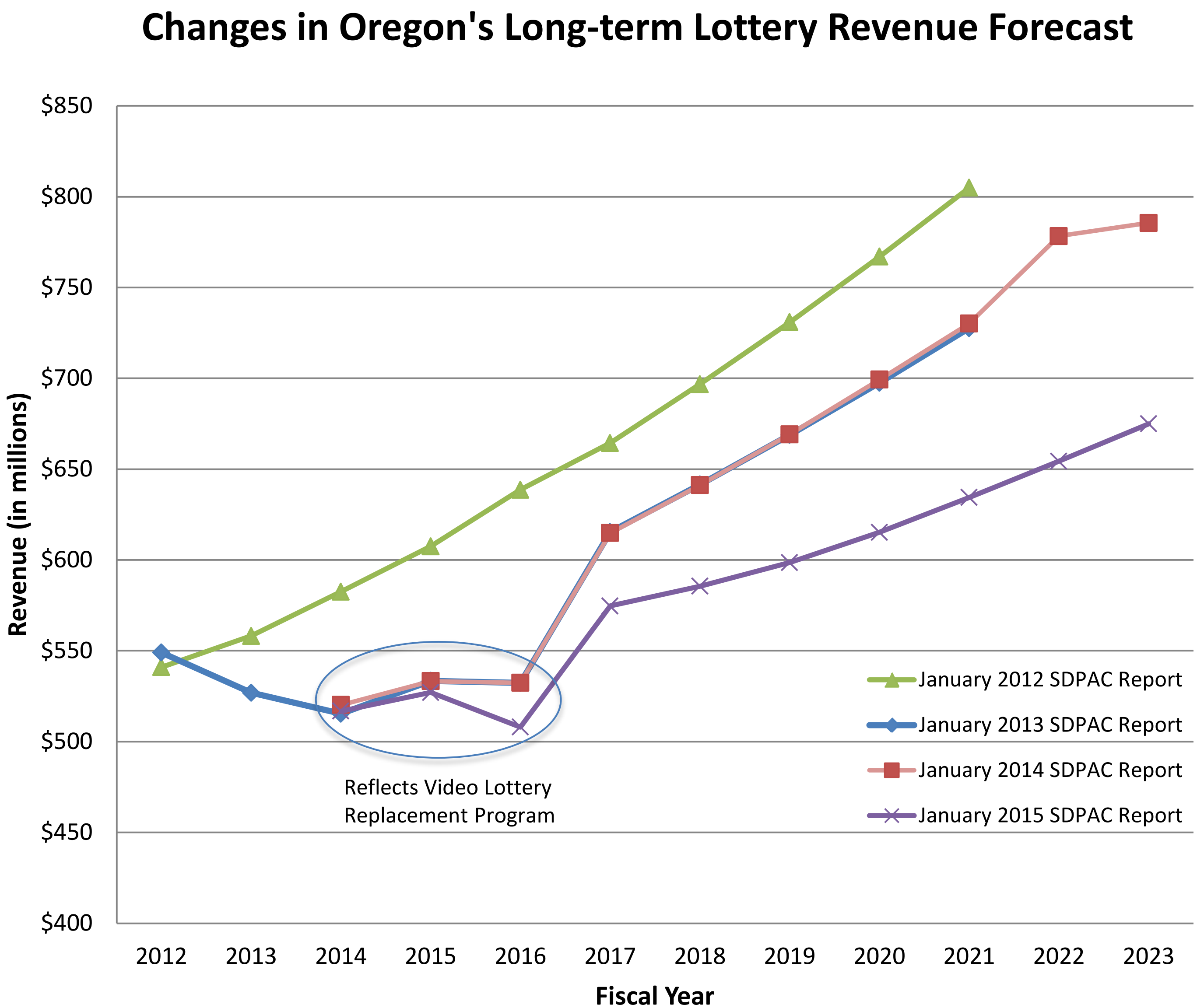
- **$1.1 billion** in bonds outstanding as of 6/30/14
- Programs funded to date include:
  - Light Rail Projects
  - State Parks
  - Drinking Water
  - Schools & Education
  - State Fair & Oregon Gardens
  - Community Loans & Grants
  - Economic & Rural Development
  - “Connect Oregon” Grants
  - Regional Port and Airport Improvements
  - Supportive Housing



Model Inputs & Assumptions

- Accounts for all Lottery debt now outstanding and planned issuance of **$195.9 million** in new lottery bonds, as authorized by the 2013 and 2014 Legislatures
- Incorporates December 2014 Lottery revenue forecast for the next eight years
- New debt issued as level debt service over 20 year term at 4.87% interest rate (average BB-20 over last 10 years plus 50 bps)
- Target based on 4x debt service coverage or maximum of 25% of net lottery revenues

Lottery-Backed Debt



Projected Lottery Revenue Bond Capacity
Over the Next Eight Years

Fiscal Year Ending June 30	Maximum Amount That Can be Issued within Debt Service Coverage Ratios (in millions)	Projected Debt Service Coverage Ratio (Times)
2015	--	4.2
2016	31	4.0
2017	208	4.0
2018	46	4.0
2019	85	4.0
2020	84	4.0
2021	61	4.0
2022	63	4.0
2023	65	4.0
Lottery Debt Capacity Over the Forecast Period	**$ 643**	

* This amount is in addition to the $195.9 million in Lottery bonds authorized by the 2013 and 2014 Legislatures

Factors that Could Impact Projected Lottery Bond Capacity

(in millions)

	Fiscal Years 2016 - 2023*	Average Per Biennium**
Base Case	**$ 643**	**$ 161**
Change in lottery revenue forecast		
10% decline	430	107
10% increase	856	214
Change in long-term interest rates		
1.0% higher	591	148
1.0% lower	702	175

* Does not Include the $195.9 million authorized by the 2013 and 2014 Legislatures
** May not total due to rounding

Net Tax-Supported Debt

Net Tax-Supported Debt Programs Include:

All

General Fund-Supported Debt Programs

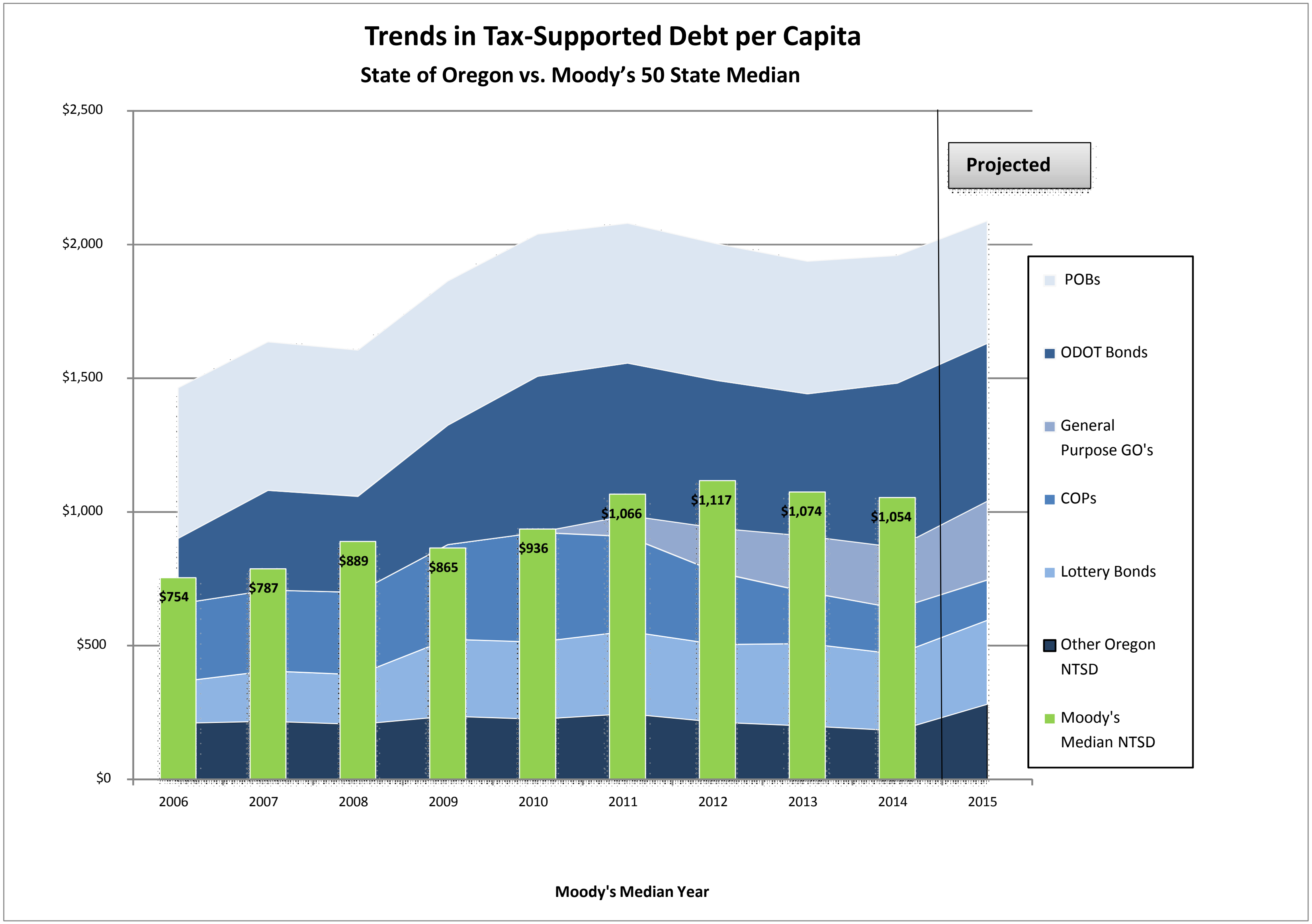
Plus

- Balance of Pension Obligation Bonds (68% of total)
- Balance of COPs and XI-Q bonds (15% of total)
- Lottery Revenue Bonds
- Highway User Tax Revenue Bonds

State of Oregon
Net Tax-Supported Debt Ratios

	Fiscal Year Ending June 30th		
	FY 2013 (Actual)	**FY 2014** (Actual)	**FY 2015** (Projected)
Net Tax-Supported Debt **(in Billions)**	$ 7.57	$7.77	$ 8.38
NTSD Per Capita	$1,933	$1,960	$2,088
NTSD as % of Personal Income	4.83%	4.73%	4.85%
Excluding Pension Obligation Bonds			
NTSD Per Capita	$1,437	$1,482	$1,631
NTSD as a % of Personal Income	3.59%	3.58%	3.79%

Net Tax-Supported Debt



Sources: Moody's State Debt Medians Reports, 2006–2014

S&P's Ranking of 50 States' Overall Liabilities

(Based on Public Debt and Pension UAAL)

State Retirement Systems And Debt Statistics: 2012

(Ranked by Per Capita Debt and UAAL)

	(%)	Increased/Decreased/Unchanged	($)					(%)		
State	Funded ratio	Funded ratio relative to prior year	UAAL (mil.)	UAAL PC	Debt (mil.)	Debt PC	Debt PC + UAAL PC	Debt PC + UAAL PC/Income PC	Debt PC+ UAAL PC/GSP PC	GO rating
Tennessee	91.5	Decreased	3,389	522	2,406	370	892	2.27	2.01	AA+/Stable
South Dakota	92.6	Decreased	638	755	126	149	905	1.99	1.64	AA+/Stable
North Carolina	95.4	Unchanged	3,881	394	7,916	804	1,198	3.11	2.50	AAA/Stable
Nebraska	78.2	Decreased	2,430	1,301	25	13	1,314	2.85	2.24	AAA/Stable
Idaho	84.6	Decreased	2,112	1,310	207	128	1,438	4.06	3.72	AA+/Stable
Texas	82.0	Unchanged	31,671	1,197	9,522	360	1,557	3.58	2.69	AAA/Stable
Oregon	92.5	Increased	1,182	301	6,428	1,636	1,936	4.81	3.47	AA+/Stable
Wisconsin	99.9	Unchanged	70	12	12,423	2,163	2,175	5.04	4.42	AA/Stable
Florida	86.4	Unchanged	20,158	1,031	23,579	1,206	2,237	5.37	5.46	AAA/Stable
Iowa	79.5	Unchanged	6,156	1,992	1,087	352	2,344	5.20	4.37	AAA/Stable
Average of states	70.9		17,882	3,155	9,640	1,325	4,479	10.15	8.64	
Median of states	65.8		12,046	2,962	4,063	1,036	3,860	8.74	7.54	

Source: Standard and Poor's U. S. Pension Report, June 24, 2014

Non Tax-Supported Debt

Non Tax-Supported Debt Programs

General Obligation Programs

- Veteran's Welfare Bonds
- Elderly & Disabled Housing Bonds
- Higher Education Facility (XI-F) Bonds
- Alternate Energy Bonds (67% of d/s)
- Oregon School Bond Guarantee Program

Direct Revenue Bond Programs

- Single & Multifamily Housing Bonds
- Economic Development Bond Bank

Conduit Revenue Programs

- Economic Development Revenue Bonds
- Oregon Facilities Authority Bonds
- Multi-Family Housing Revenue Bonds

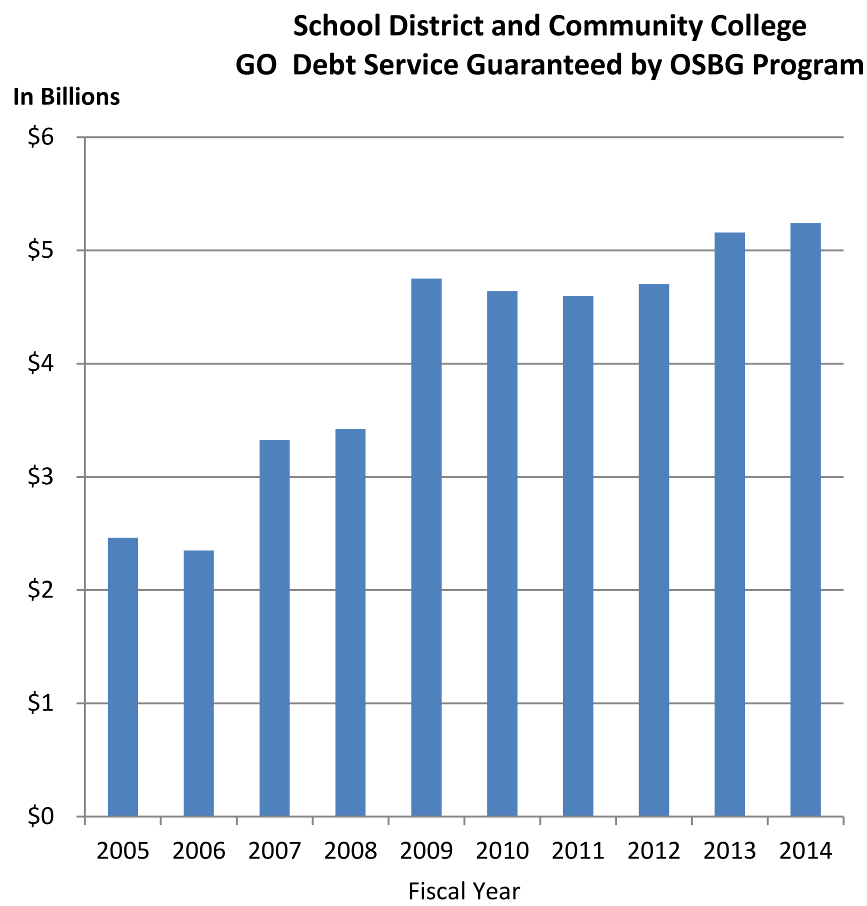
Debt Policy Issues Before the 2015 Legislature

- SB 303 - Requires State Treasurer oversight of future fund diversion agreements entered into by the Department of Education to provide a state guarantee on local district Pension Obligation bonds

- Determination as to which state agency will provide on-going administrative oversight for the state GO bond programs funding projects at independent universities

State Guarantees of Oregon School District and Community College Bonds

- The **Oregon School Bond Guaranty** (OSBG) program was created in 1998 via Constitutional amendment as a way to enhance the credit rating and lower the borrowing cost on General Obligation (GO) school bonds
- State pledges its full faith and credit to payment of a qualifying school district or community college's GO debt service when due, which allows these bonds to receive the same credit rating as the State's GO bonds
- The State Treasurer is authorized to use State School Aid to repay any draw on state funds used to make an OSBG-related debt service payment
- The OSBG program grew dramatically since 2008 due to improved state credit ratings and the elimination of bond insurance as an alternative means of credit enhancement

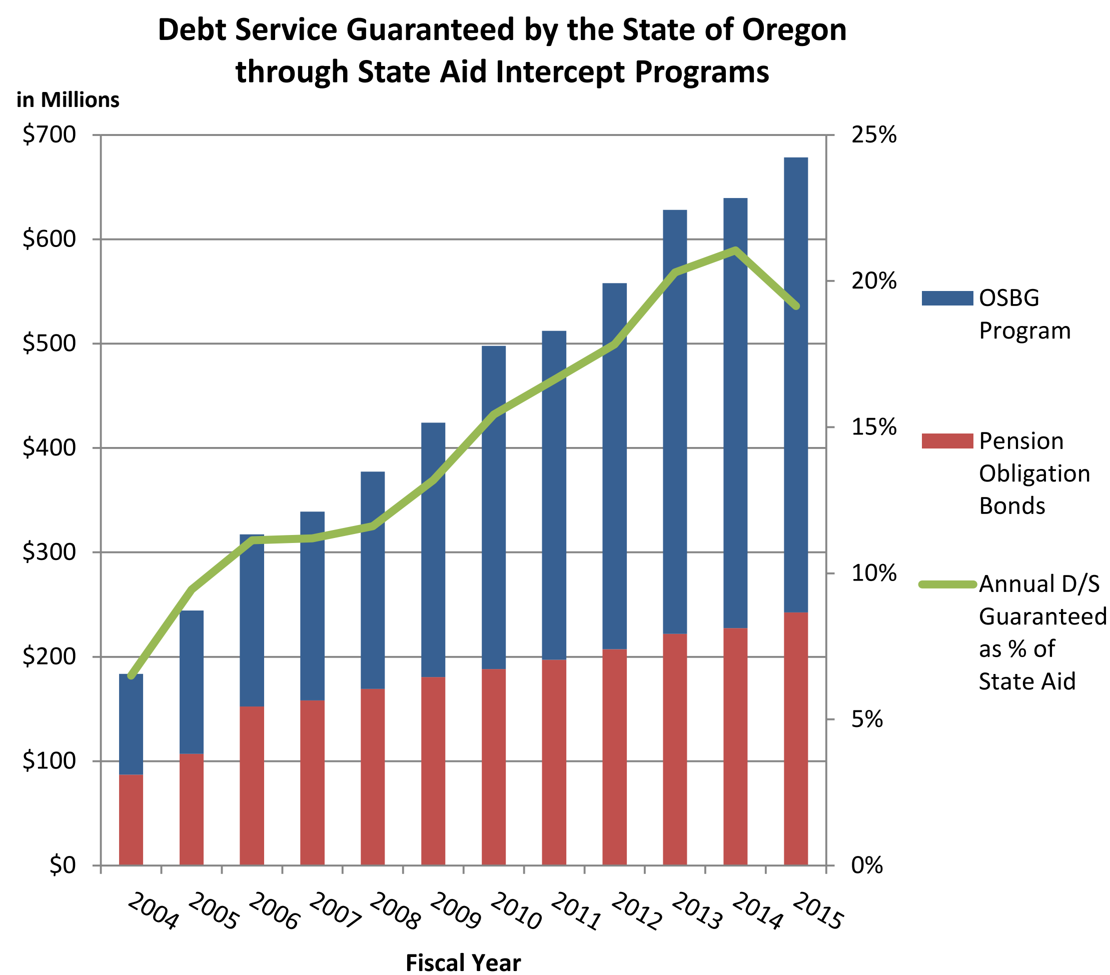


State Guarantees on Oregon School District and Community College POBs

- In 2001, the Legislative Assembly authorized the Department of Education to enter into State School Aid fund diversion agreements as a means of improving the creditworthiness of Pension Obligation Bonds (POBs) issued by Oregon school districts and community colleges to prepay their accrued unfunded PERS liabilities
- Under these diversion agreements, the State Board of Education makes POB debt service payments directly to the POB bond trustee out of annual state aid funds allocated to participating school districts and colleges
- Between 2002 and 2007, $3.1 billion was issued in nine separate pooled POB borrowings with this fund diversion provision
  - Like the OSBG program, the State guarantee of debt service repayment greatly enhanced the credit rating and lowered the borrowing cost on these bonds
  - The annual debt service on these bonds grows by approximately 4.7% each year until the balance of bonds are retired in FY 2028
- Under current state law, the State Treasurer's office **does not** review or approve these POB fund diversion agreements

Combined Annual State Guaranteed Debt Service of Oregon School Districts and Community Colleges

- Three school districts currently have combined annual State guaranteed debt service (GO and POB) that exceeds their annual allocation of State school aid
- Over the past year, the State Treasurer's office tightened OSBG's administrative rules to assure that qualifying district's combined annual guaranteed debt service does not exceed **80%** of its annual State school aid
- The State Treasurer will also seek legislation in 2015 to require State Treasurer's office review and approval of all future POB fund diversion agreements to assure that the State does not overcommit this resource on a combined program basis



Management of State GO Bond Programs for Independent Universities

- Since the passage of SB 270 in 2013, which authorized the dissolution of the Oregon University System (OUS) and the establishment of independent universities with governing boards, the State Treasurer's office has encountered several unresolved legal and administrative issues related to future issuance of State XI-F(1) and XI-G GO bonds for independent universities
  - SB 270 did not assign a state agency to coordinate the on-going administrative functions required to effectively manage this large, complex State GO bonding program
- ORS 286A.005(2) authorizes the State Treasurer to issue state bonds (whether new money or refunding bonds) upon request by a related state agency
  - The recent effort by the State Treasurer's office to take advantage of low interest rates to refund approximately $145 million in outstanding XI-F(1) and XI-G GO bonds revealed the unwieldy logistics involved in gaining the timely bond issuance authorization now required from multiple independent universities
- It has also became clear that there is a need for one central state agency to provide administrative oversight with regards to bond proceeds disbursement, as well as related legal, accounting and tax law compliance for future XI-F(1) and XI-G GO bonds for independent universities

Management of State GO Bond Programs for Independent Universities (continued)

- In the past, the State's Higher Ed GO bond program duties were legally assigned to the Board of Higher Education, with much of the day-to-day administrative activities performed by staff within the OUS Chancellor's office
- At the time SB 270 was adopted, it was assumed that all of these bond program functions could be performed by the same OUS staff, but through the new University Shared Services Enterprise (USSE)
  - DOJ has subsequently determined that since the USSE is not a state agency (it is administratively part of Oregon State University), it cannot directly serve in this capacity
- The State Treasurer's office recommends that legislation be adopted as soon as possible assigning either DAS or the Higher Education Coordinating Commission as the state agency with oversight responsibility for these GO bonding programs
- Resolution of this matter early in the 2015 session is critical for the sale of $117 million in authorized XI-G GO bonds to occur as planned in early May 2015
  - Once a lead state agency has been assigned, it may be possible to establish MOUs between the selected agency and the USSE with regards to the delegation of many of the day-to-day debt administrative functions

Conclusions

- Tax-exempt interest rates have declined in recent years, allowing the State to issue new money and refunding bonds at historically low interest rate levels
- Based on current assumptions regarding the sale of $843.5 million in authorized GO bonds in FY 2015, future interest rates, and projected long-term revenue growth, there is an additional $3.9 billion in General Fund-supported debt capacity over the next four biennia while remaining within the SDPAC's 5% debt service target limit
  - The Commission has historically recommended that the State conserve debt capacity by averaging out this GF bond authorization over time
  - For the 2015-17 biennium, this averaging approach suggests a maximum GF debt capacity of $**974 million**

Conclusions (continued)

- Based on the December 2014 forecast of Lottery revenues and the planned sale of $195.9 million in Lottery bonds in 2015, there remains $643 million in Lottery bond capacity over the next four biennia
  - Based on the debt capacity “averaging” approach historically recommended by the Commission, overall 2015-17 Lottery bond capacity is **$161 million**
  - Given the continued drop in projected lottery revenue, the Commission should urge that the Legislature to exercise extreme caution in authorizing future Lottery bonds

Conclusions (continued)

- While Oregon's net tax-supported debt ratios remain above national averages, the State's overall liability (which is the sum of both its public debt and its unfunded PERS liability) is well below national averages
- The growing contingent liability represented by State's credit enhancement of the debt of school districts and community colleges through State School Aid intercept programs warrants the tightening of the oversight of future POB fund diversion agreements to assure that the State's General Fund is never put at risk
- Quick resolution of the issue of program oversight for independent university bond sales early in the 2015 session will allow the State Treasurer to sell authorized XI-G GO bonds in May 2015