

Joint Committee on Ways and Means Subcommittee on Capital Construction

Overview of the 2015 State Debt Policy Advisory Commission Report



**Office of the State Treasurer
Debt Management Division**

March 20, 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



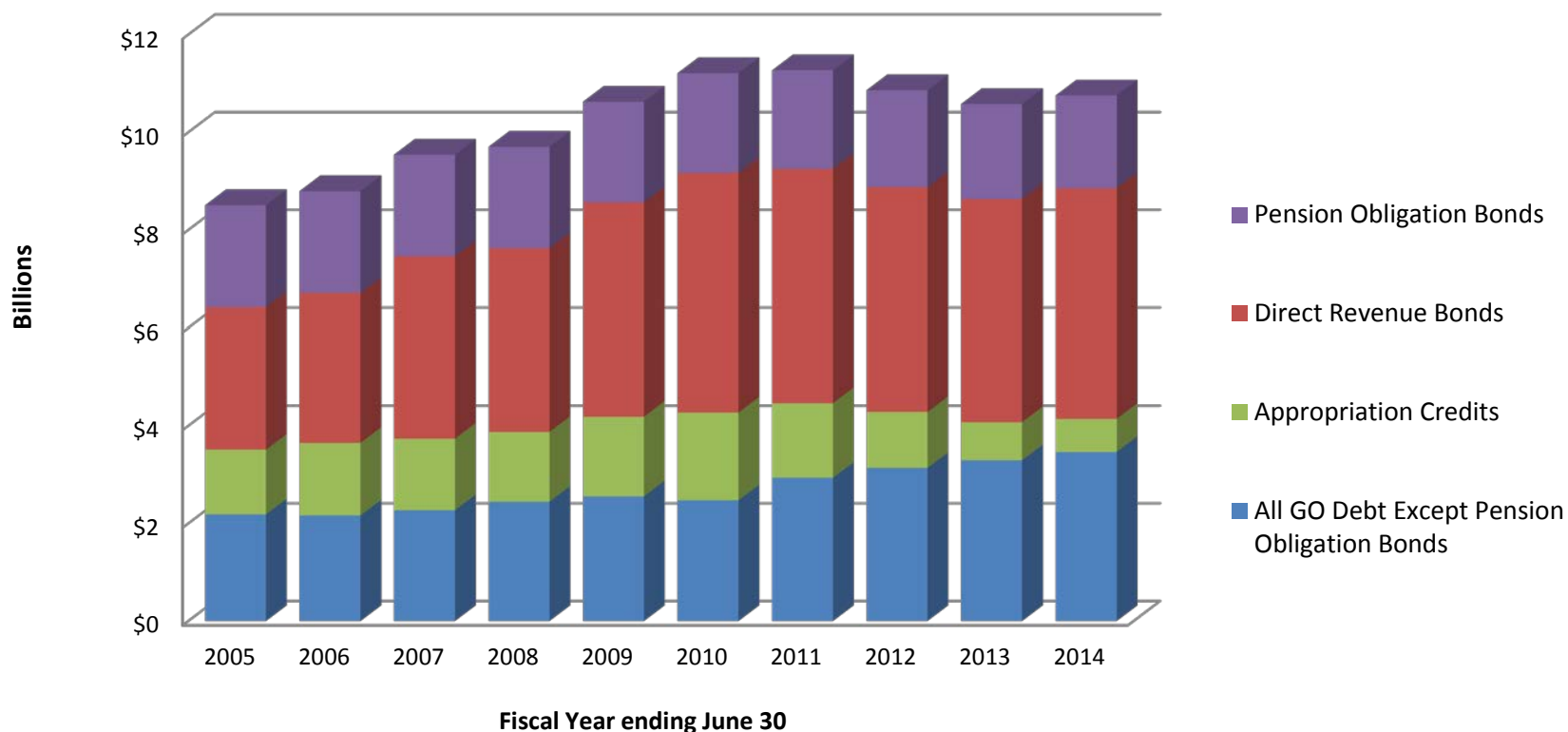
Debt Capacity Concepts

Four Types of Long-Term Debt

| | |
|------------------------------------|---|
| 1. General Obligation Bonds | <ul style="list-style-type: none">• Requires voter approved constitutional amendment• Pledges the full faith & credit of the State• Includes both GF-supported <u>and</u> non GF-supported bond programs |
| 2. Direct Revenue Bonds | <ul style="list-style-type: none">• 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 | <ul style="list-style-type: none">• 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 | <ul style="list-style-type: none">• 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 |



Oregon's Bonded Indebtedness Over the Past Decade



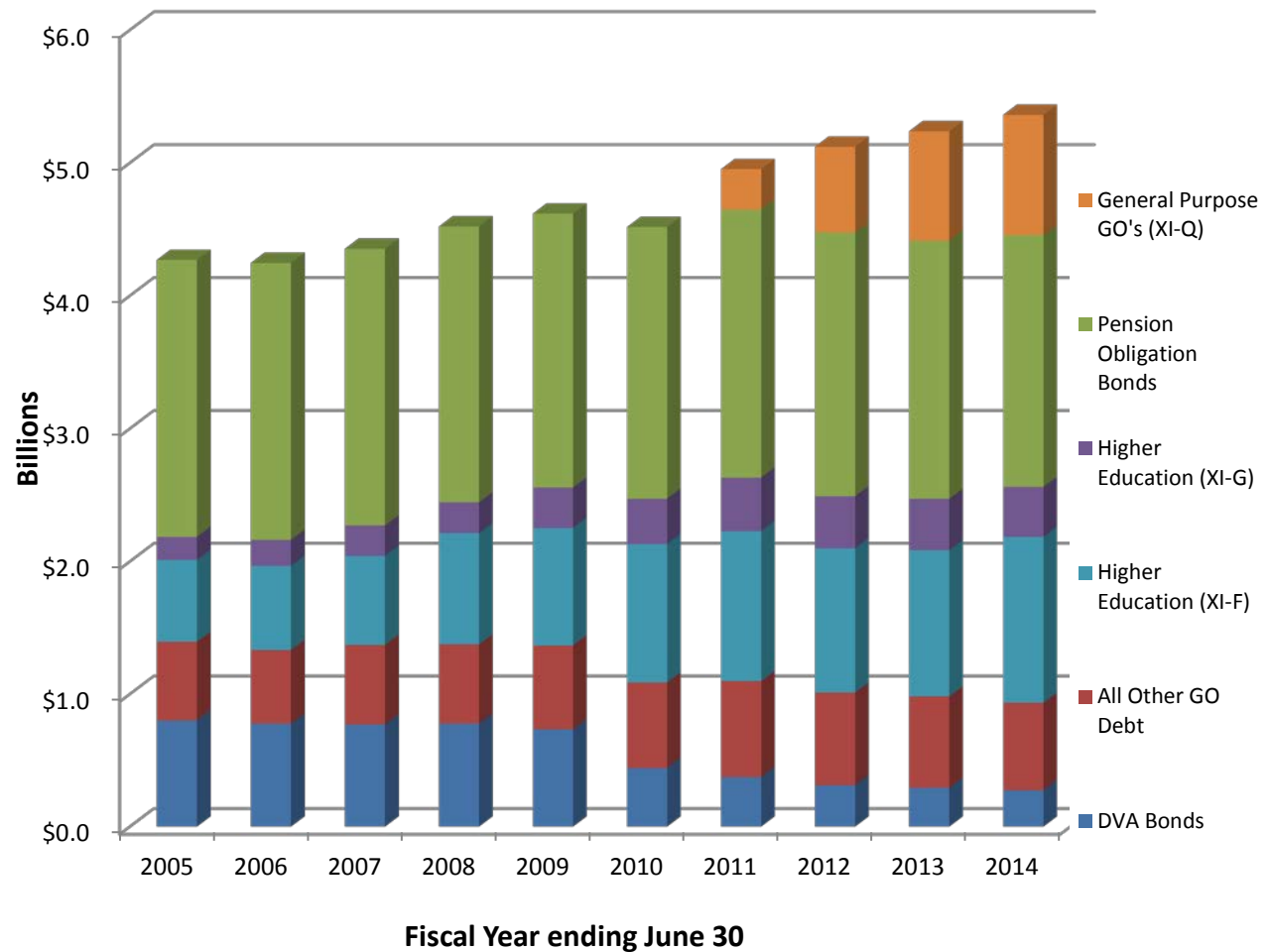
- The State's overall debt levels rose steadily from FY 2005 through FY 2010, but has remained relatively stable since then, as existing debt retirement has generally kept pace with new debt issuance



Debt Capacity Concepts

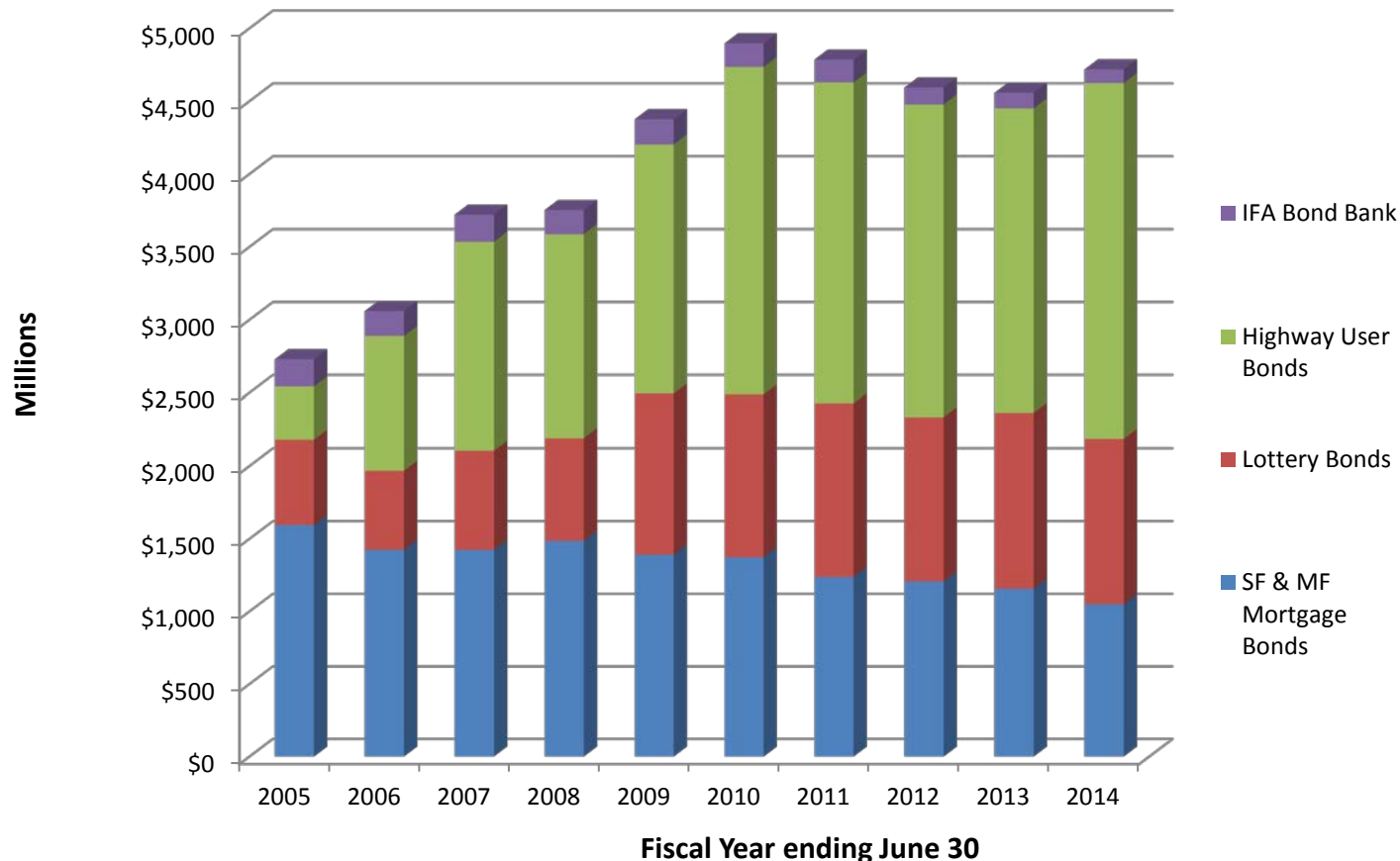
- In FY 2004, the State issued \$2.4 billion in Pension Obligation Bonds, of which \$1.9 billion remained outstanding at the end of FY 2014
- In recent years, most new GO bonds were issued to fund building projects at public universities and community colleges
 - \$1.9 billion of this type of debt was outstanding as of June 30, 2014
- Since FY 2011, the State has issued \$472 million in XI-Q bonds to refund existing COPs, saving to date over \$70 million in interest costs over the life of these bonds

State General Obligation Debt Outstanding



Debt Capacity Concepts

Direct Revenue Bonds Outstanding by Bond Program

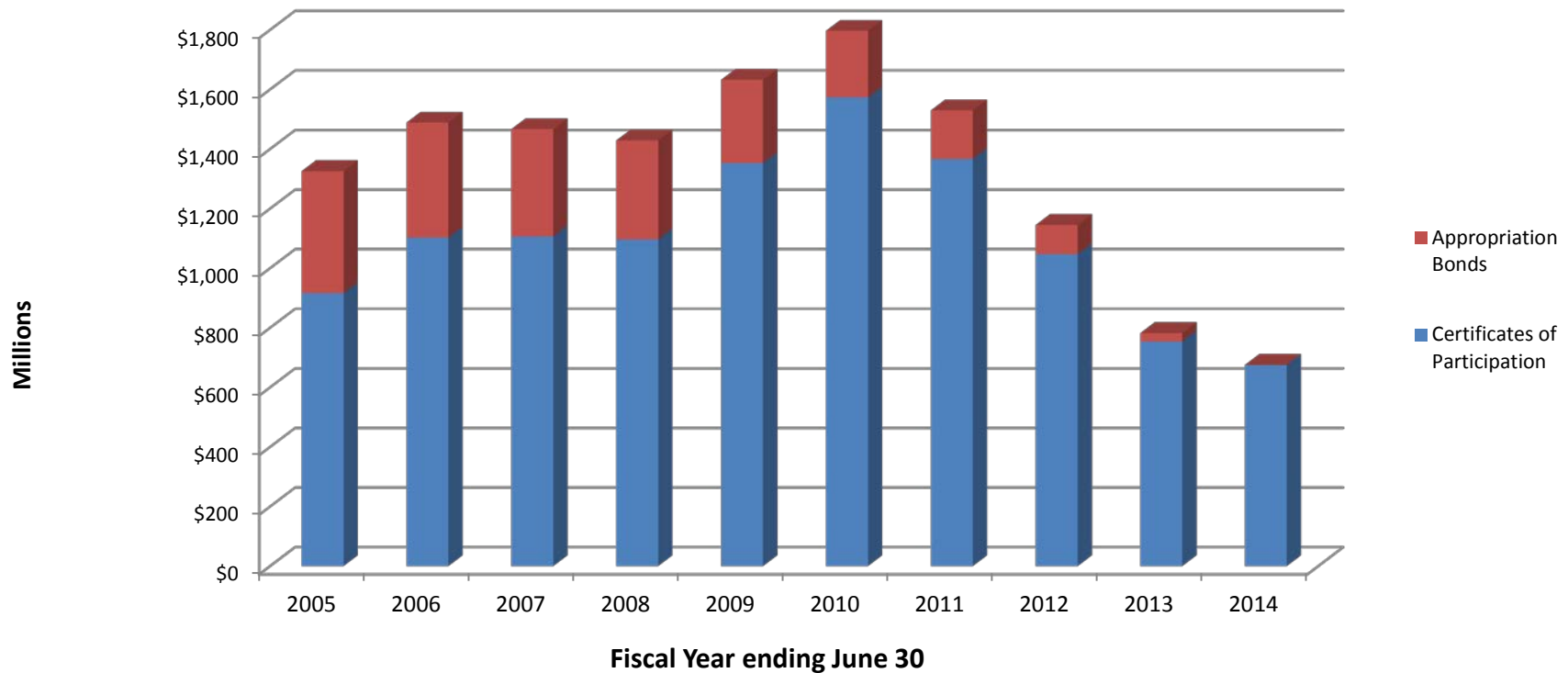


- The issuance of \$2.8 billion in Highway User Tax Bonds to fund ODOT's multi-year bridge and highway improvement and congestion management programs is responsible for the majority of the growth in outstanding state revenue bonds
- With the introduction of video line games in 2005, both net Lottery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



Debt Capacity Concepts

Outstanding Appropriation Credits



- 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



Four Debt Capacity Categories

| | |
|---------------------------------------|--|
| 1. General Fund-Supported Debt | <ul style="list-style-type: none">• SDPAC Recommended Target Limit -- 5% of General Fund Revenues |
| 2. Lottery-Backed Debt | <ul style="list-style-type: none">• Legal Bond Covenant Limit: 4x Coverage (no more than 25% of net lottery revenues)• Moral obligation pledge of State |
| 3. Net Tax-Supported Debt | <ul style="list-style-type: none">• National bond rating agency perspective.• States compared with each other using “apples-to-apples” measurement approach |
| 4. Non Tax-Supported Debt | <ul style="list-style-type: none">• 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

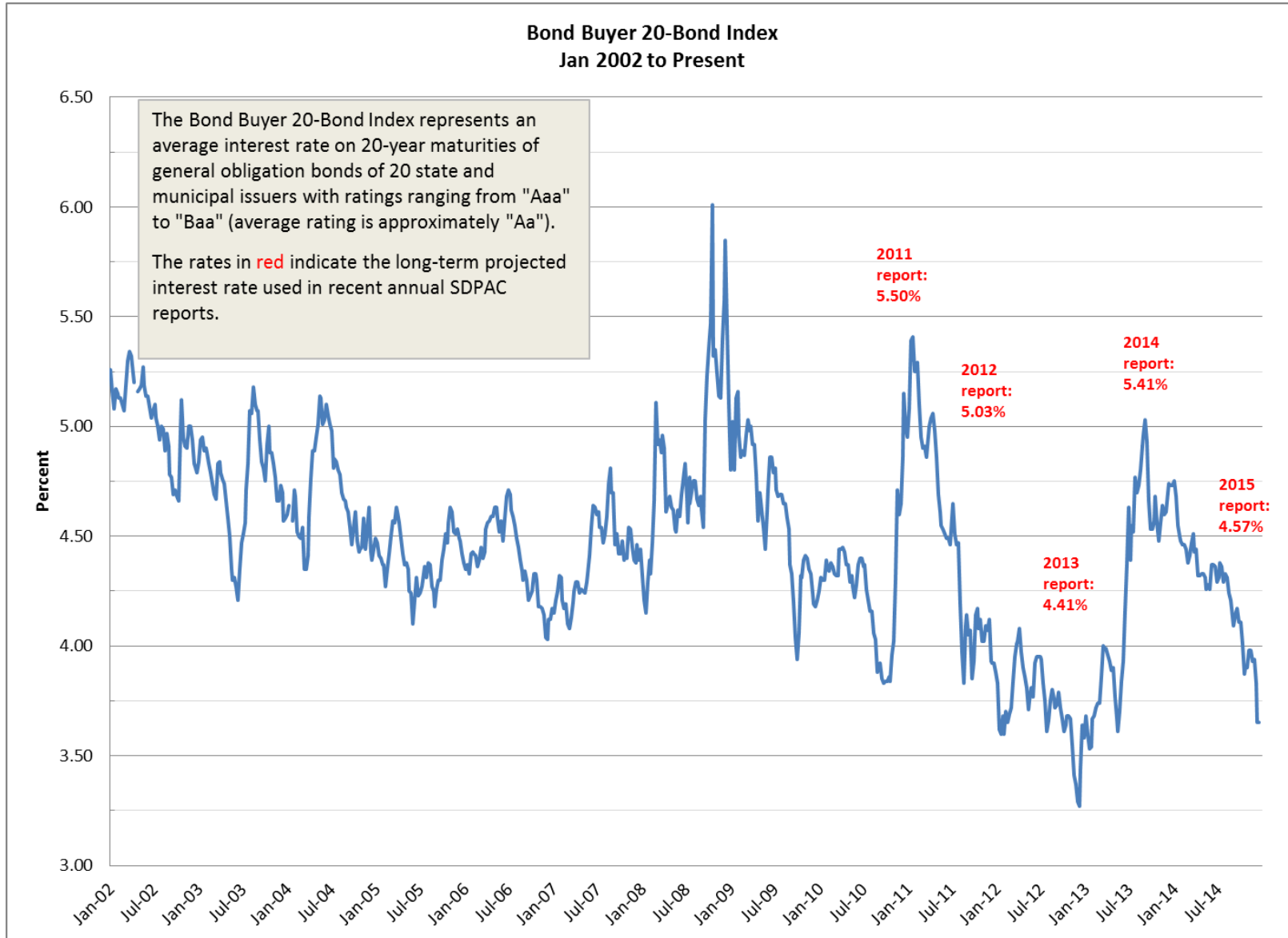


Model Inputs & Assumptions

- 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

| | <u>FY 2016 – FY 2023*</u> | <u>Per Biennium **</u> |
|---|-------------------------------|------------------------|
| Base Case | \$ 3,896 | \$ 974 |
| <u>Change in General Fund forecast</u> | | |
| 10% decline | 3,139 | 784 |
| 10% increase | 4,652 | 1,163 |
| <u>Change in interest rate forecast</u> | | |
| 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

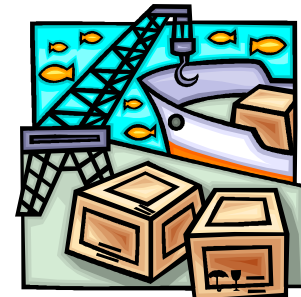
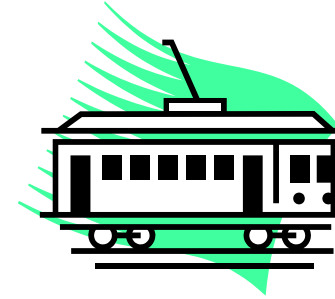
** May not total exactly due to rounding



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
 - Community Health Centers



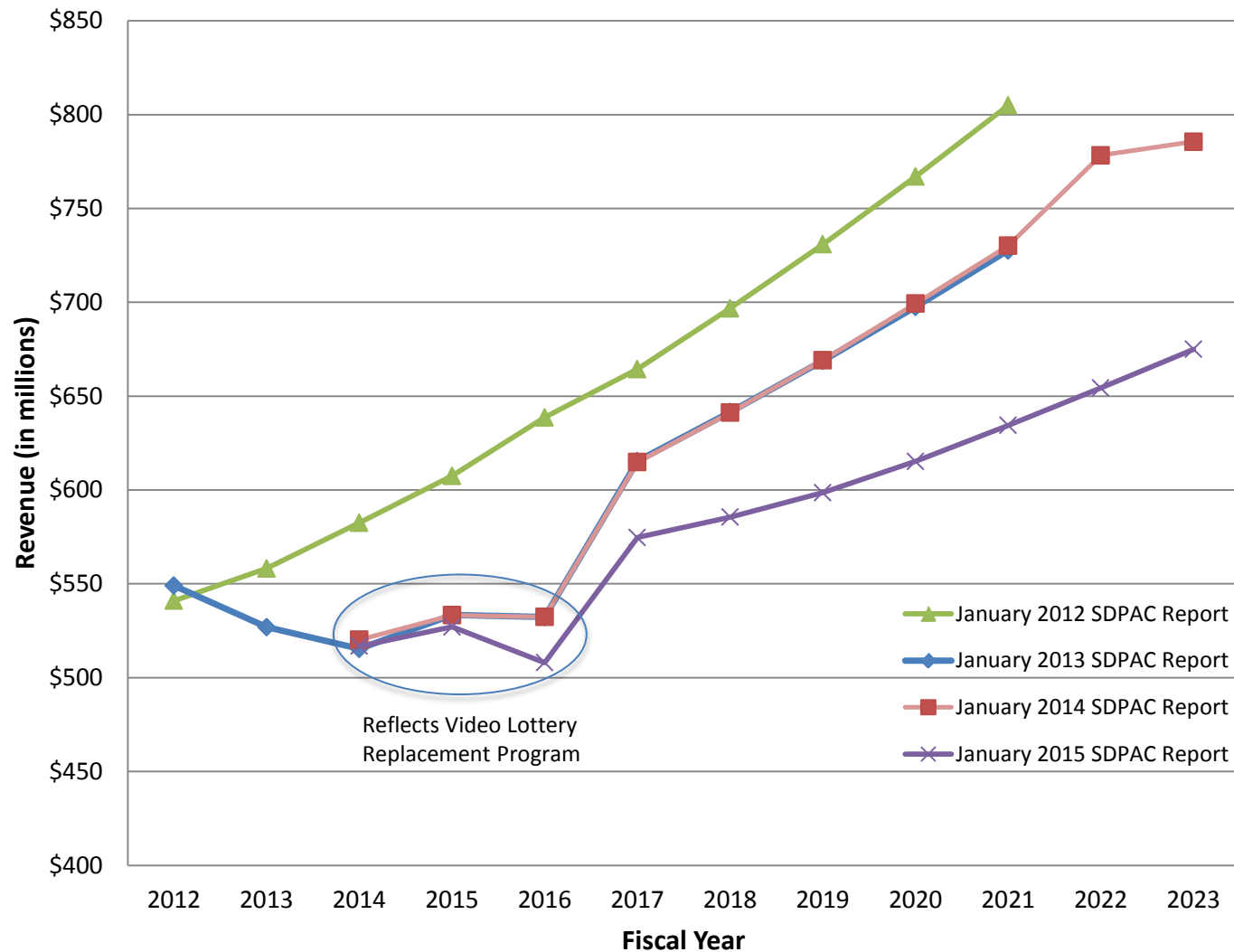
Model Inputs & Assumptions

- 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

Changes in Oregon's Long-term Lottery Revenue Forecast



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)

| | <u>Fiscal Years</u> <u>2016 - 2023*</u> | <u>Average Per</u> <u>Biennium**</u> |
|---|--|---|
| Base Case | \$ 643 | \$ 161 |
| <u>Change in lottery revenue forecast</u> | | |
| 10% decline | 430 | 107 |
| 10% increase | 856 | 214 |
| <u>Change in long-term interest rates</u> | | |
| 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



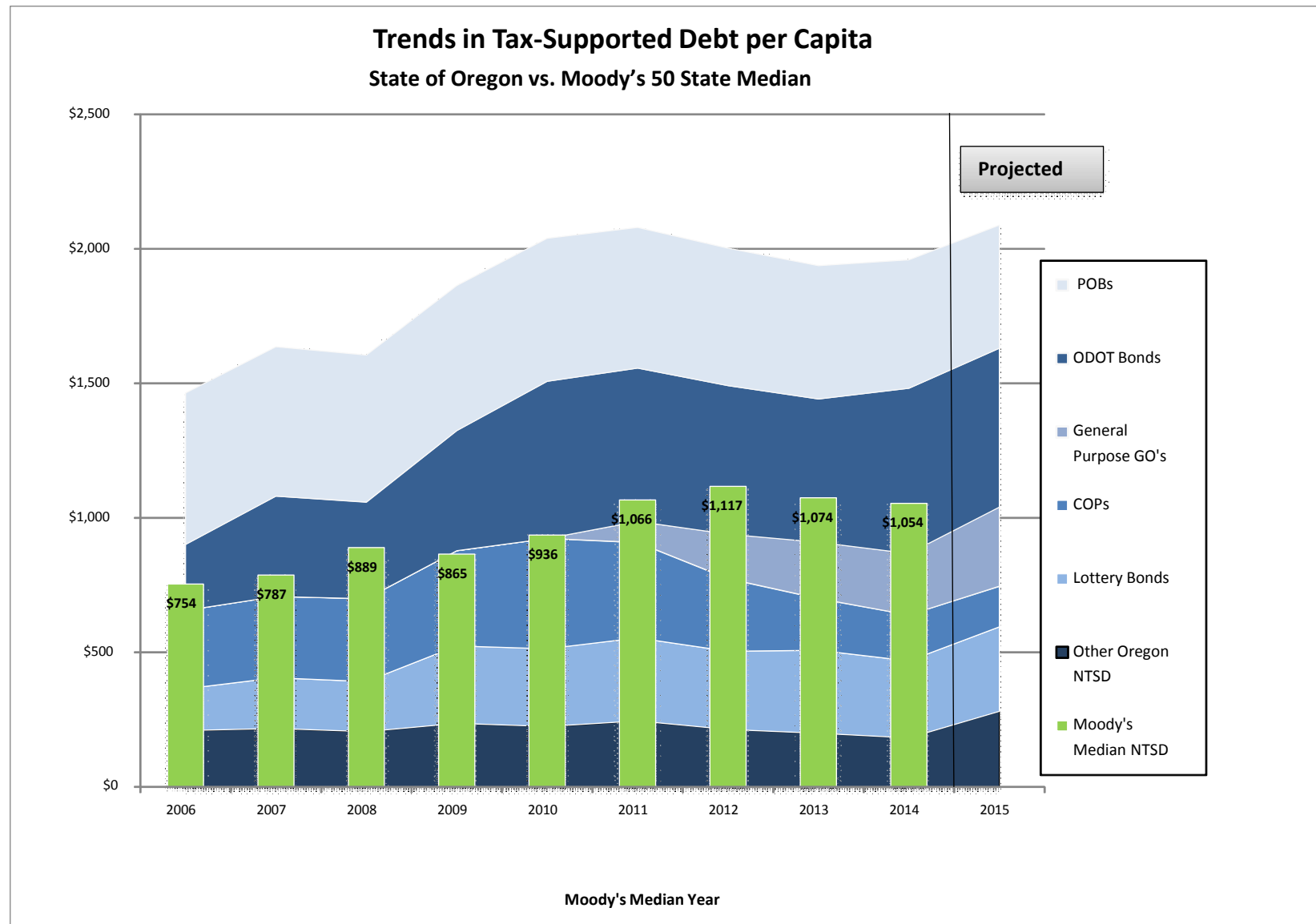
State of Oregon

Net Tax-Supported Debt Ratios

| | Fiscal Year Ending June 30 th | | |
|--|--|---------------------|------------------------|
| | 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% |
| <i>Excluding Pension Obligation Bonds</i> | | | |
| 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



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 become 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 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 either a third party trustee and/or 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
- 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

