



UPDATE ON STATE DEBT

EXECUTIVE APPROPRIATIONS COMMITTEE
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ISSUE BRIEF

SUMMARY

One of the state's primary tools to finance large capital projects (buildings and highways) is general obligation (GO) bonds. This year, Utah will issue approximately \$40 million of GO bonds for buildings as authorized in House Bill 4, 2011 General Session (General Obligation Bonds Authorizations). In addition, the Treasurer's Office and the state's financial advisors are considering some refunding of earlier bonds.

The state's constitutional debt limit caps total general obligation debt at 1.5 percent of the value of the state's taxable property. After a four percent decline in taxable property values a year ago, values have dropped another two percent in the most recent estimate. Despite the drop in property values, the state's debt as a percent of property values is gradually decreasing because the amount of debt being issued is less than the amount of debt being paid off. The Legislature did not authorize additional bonding in the 2012 General Session.

As a result of increased bonding for highway projects and a decrease in property value, Utah's per capita general obligation debt reached a historical high of approximately \$1,240 in FY 2012. While transportation revenues will be sufficient to pay debt service on existing and anticipated bonds, current revenue estimates do not support additional bond- or cash-funded highway projects until FY 2015.

DISCUSSION AND ANALYSIS***Property Values and the Constitutional Debt Limit***

The state's constitutional general obligation debt limit is 1.5 percent of the value of taxable property. The most current numbers indicate that the fair market value of Utah property is \$275 billion (a 2 percent decline from last year), which limits general obligation debt to \$4.1 billion.

By practice, legislative debt policy keeps outstanding principal below 85 percent of the constitutional debt limit. This policy provides the state flexibility to respond to unforeseen circumstances such as natural disaster and prevents the state from going over the limit should property values decline. In July 2011, we were at 87 percent of the limit; we are currently at 82 percent of the limit.

Figure 1, on page 2, includes bond issuances of \$40 million in FY 2013 and \$100 million in FY 2014 to finish road and building projects. Assuming an additional 1.5 percent decline in FY 2014 property values and slight growth in property values thereafter, the figure estimates the state will be at 77 percent of the constitutional debt limit in FY 2014 and 68 percent in FY 2015. The line graphs are cumulative. While bonding for buildings has increased outstanding debt since FY 2009, the main influence has been transportation.

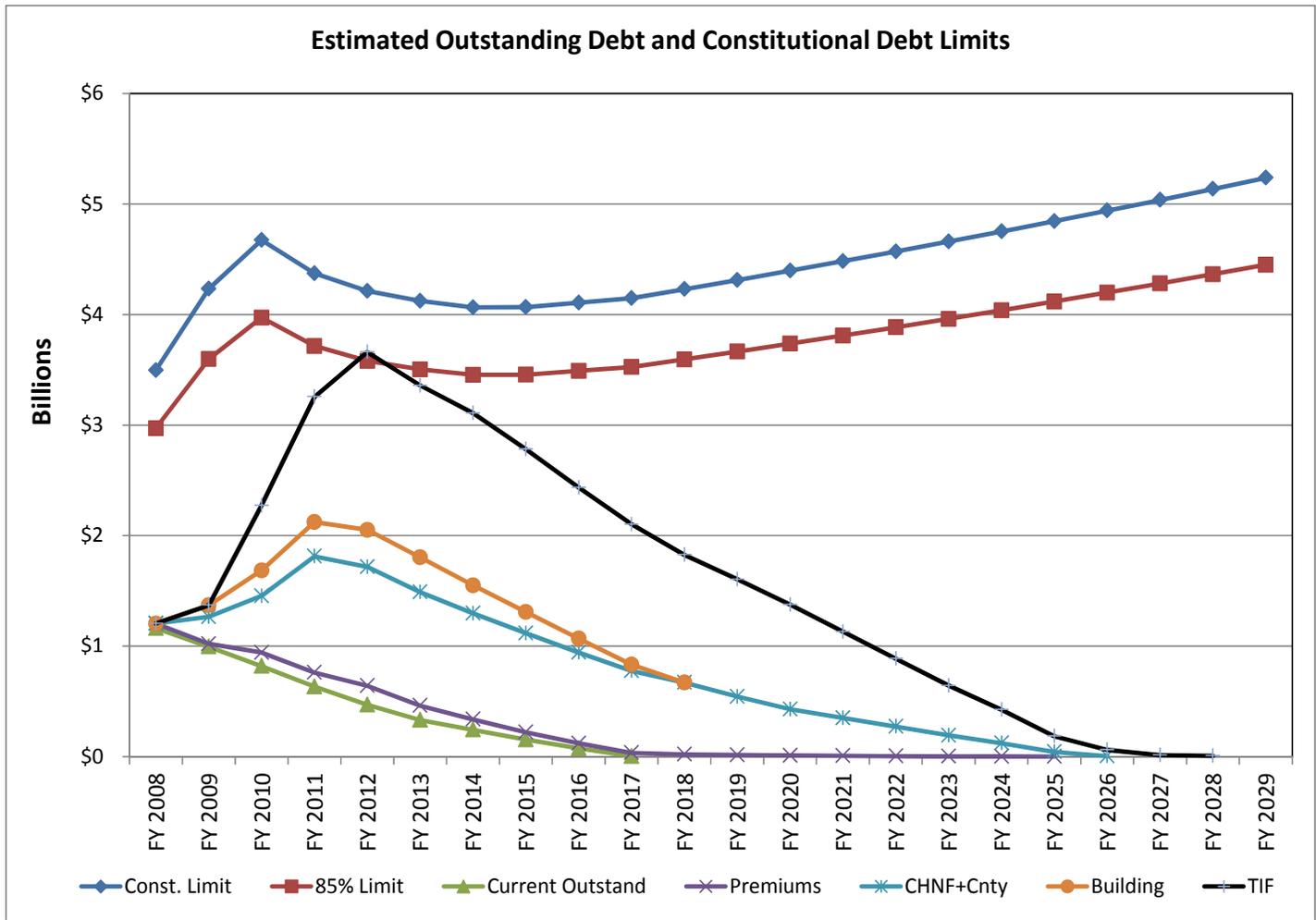


Figure 1

Calculation of Constitutional Debt Limit

Utah code clarifies that the constitutional limit should be calculated using 100 percent of the fair market value of taxable property from the last assessment. However, neither the constitution nor statute precisely defines how to make the calculation. Specifically neither is clear as to:

1. *What constitutes the “last” assessment of property?* Is the annual Tax Commission report sufficient or should up-to-date property estimates be used?
2. *What is included in assessed property?* Should land assessed under the Farmland Assessment Act be included at fair market value and/or are there other properties not currently being assessed that should be?
3. *What property tax projections will determine estimated future debt limits?* As the debt limit is a percent of property values, projecting a future debt ceiling requires an estimate of future fair market property values. Currently, taxable property value estimates used in public education calculations are also used to estimate future debt limits.

The Analyst recommends the Legislature consider legislation to clarify these three questions.

Utah's General Obligation Bond Debt

GO bonds pledge the “full faith, credit, and resources of the state.” Each year, Utah appropriates an amount sufficient to pay GO principal, interest, and fees in order to avoid levying a state property tax. Utah has never defaulted on a bond issuance nor resorted to a property tax levy to pay debt service.

Debt per capita represents the amount of outstanding principal each Utah citizen would owe at a moment in time. Utah’s per capita general obligation debt peaked at approximately \$1,240 in FY 2012 (see Figure 2). Debt per capita spiked in FY 2003 as a result of the I-15 reconstruction project in Salt Lake County and then declined over the next five years as Utah paid off the debt and cash-funded infrastructure. The current spike in debt per capita is a result of increased bonding for highway projects including the reconstruction of I-15 in Utah County and the Critical Highway Needs program. Figure 3 shows Moody’s Investor Service’s analysis of Utah’s debt per capita compared to other AAA-rated states as of FY 2011.

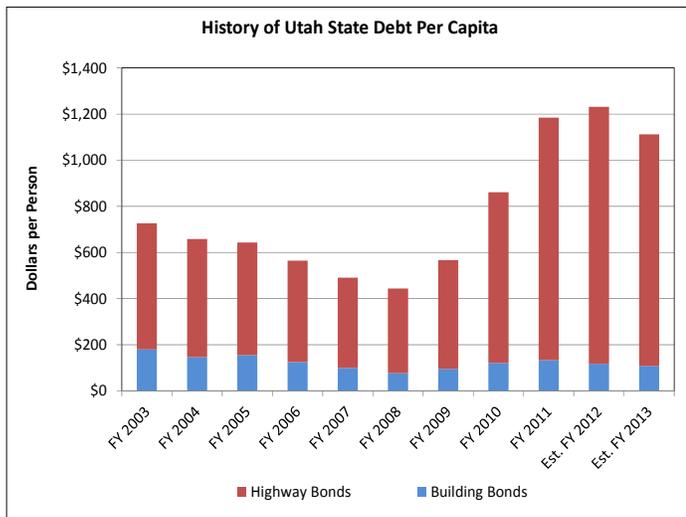


Figure 2

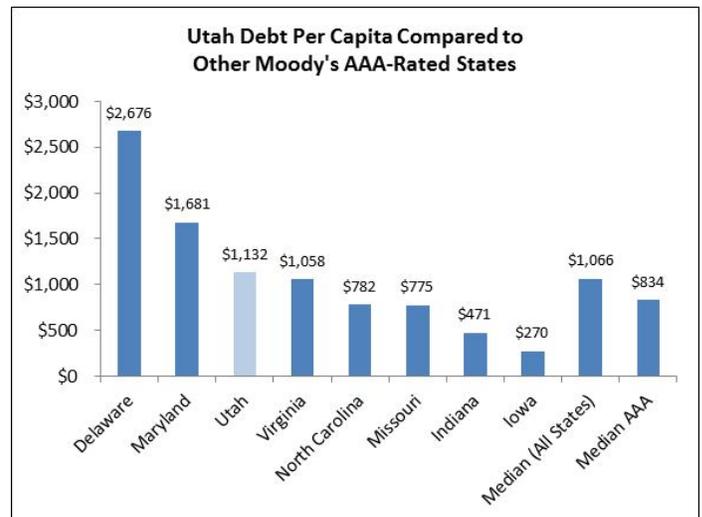


Figure 3

Historically the state issues GO bonds with 15 year maturities for highways and six year maturities for buildings. These short maturities allow the state to pay off almost three-quarters of its debt in 10 years. In FY 2014, the state will pay off \$315 million of bond principal and pay \$129 million of interest on GO bond debt. Figure 4, below, shows Moody’s analysis of Utah’s debt service ratio compared to other AAA-rated states as of FY 2011. This ratio compares debt service payments to available revenues. Figure 5 displays the current debt service schedule, but does not reflect unissued bonds authorized by the Legislature.

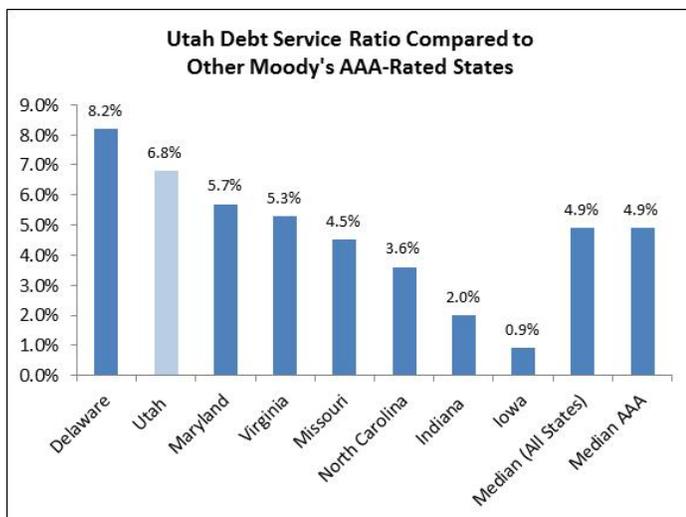


Figure 4

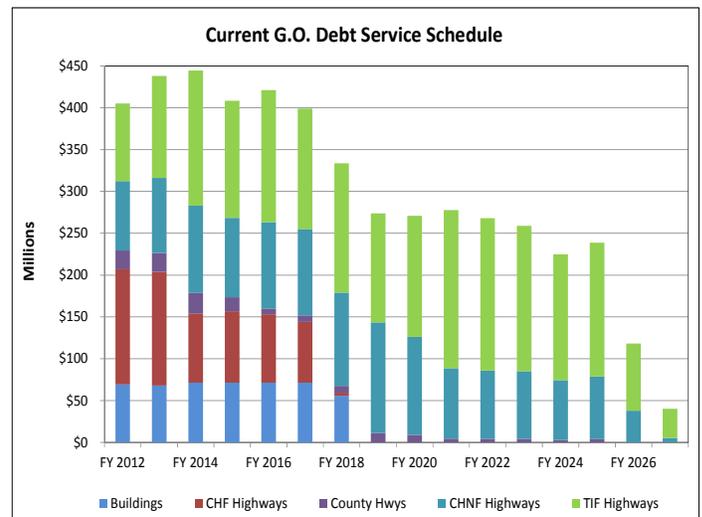


Figure 5

CONCLUSION AND RECOMMENDATION

With outstanding debt currently at 82 percent of the constitutional limit and the state paying off \$315 million of bonds in FY 2014, the state has bonding capacity to complete authorized capital projects. Transportation revenues will be sufficient to pay debt service on existing and anticipated bonds. However, significant capacity to bond or cash-fund new transportation projects, beyond *Transportation Funding Revisions* (S.B. 229, 2011 G.S.) revenue, will not likely exist until FY 2015.

The Analyst recommends the Legislature consider legislation to:

1. Clarify how to calculate the constitutional debt limit, including what is meant by “last assessment” of taxable property, what should be included in assessed property, and what property tax projections will be used to estimate future debt limits.
2. Codify the priority of payments to debt service obligations. Bond rating agencies have indicated this helps strengthen a state’s credit rating, while recognizing that Utah’s rating is already as high as possible.