DEBT SERVICE OVERVIEW

EXECUTIVE APPROPRIATIONS COMMITTEE
STAFF: BRIAN WIKLE

ISSUE BRIEF

DEBT SERVICE BUDGET

Debt service is made up of interest and principal due on the state's bonded indebtedness. The state uses bonds to finance large capital expenditures, including new facility construction, major remodeling, and highway projects. General Obligation (G.O.) bonds are backed by the full faith and credit of the state. Lease revenue (L.R.) bonds are secured by dedicated revenue streams such as enterprise fund revenue or lease payments. The debt service line item in appropriations bills combines service for G.O. and revenue bonds.

The state paid $454.7 million in debt service in FY 2015 and $467.5 million in FY 2016, and the Legislature appropriated $445.5 million for debt service for FY 2017. Table 1 shows sources of finance for debt service for FY 2015 actual, FY 2016 estimated, and FY 2017 appropriated. Note that figures are rounded to the nearest hundred.

Table 1: Debt Service Sources of Finance

Source of Finance	FY 15 Actual	FY 16 Estimated	FY 17 Appropriated
General Fund	54,473,100	54,535,800	54,535,800
Gen. Fund, One-time	14,203,600	14,139,000	13,991,000
Education Fund	17,222,400	17,221,800	17,221,800
TIF of 2005	326,466,900	348,420,200	325,450,000
Federal Funds	15,758,900	15,758,900	15,758,900
Ded. Credits Revenue	24,782,800	25,089,100	25,089,100
County of 1st Class	16,498,900	6,383,600	7,409,000
Transfers	(14,139,000)	(14,139,000)	(14,214,000)
Beginning Nonlapsing	7,652,800	8,646,100	8,567,700
Closing Nonlapsing	(8,646,100)	(8,567,700)	(8,335,200)
Lapsing Balance	398,200		
Total	454,672,500	467,487,800	445,474,100
G.O.	*428,269,800*	*440,477,400*	*418,384,600*
L.R.	*26,402,700*	*27,010,400*	*27,089,500*

GENERAL OBLIGATION (G.O.) BONDS

Outstanding G.O. Bonds. Table 2 shows the State's current outstanding G.O. bond indebtedness broken out by buildings and highways. The State's FY 2017 G.O. bond indebtedness is $2.50 billion and the State made FY 2017 principal payments totaling $324.9 million on July 1, 2016, the first day of the fiscal year. The table does not include approximately $473.5 million in bonds (including issuance costs) authorized by the Legislature for construction of a prison but not yet issued. It also does not include about $63.7 million authorized for highway projects but that the Department of Transportation does not need as projects were completed ahead of schedule and the department received greater than anticipated revenue; the Fiscal Analyst's Office recommends rescinding this authorization as shown in Senate Bill 95, 2016 General Session, that was not enacted.

Table 2: General Obligation Bond Payments and Principal Outstanding

	Series	Original Amount	Final Maturity Date July 1	July 1, 2016 Principal Outstanding	July 1, 2016 Principal Payment	July 1, 2017 Principal Outstanding
Capital Facility Projects	2010A	79,710,000	2016	45,710,000	45,710,000	0
	2011A	46,860,000	2017	46,860,000	20,000,000	26,860,000
	2012A	33,240,000	2017	31,195,000	3,050,000	28,145,000
Highway Projects	2004A*	314,775,000	2016	57,405,000	57,405,000	0
	2009A	394,360,000	2018	75,795,000	25,265,000	50,530,000
	2009C	363,630,000	2018	207,525,000	69,165,000	138,360,000
	2009D	491,760,000	2024	491,760,000	0	491,760,000
	2010A	333,280,000	2017	74,330,000	35,415,000	38,915,000
	2010B	621,980,000	2025	621,980,000	0	621,980,000
	2010C*	172,055,000	2019	172,055,000	28,510,000	143,545,000
	2011A	563,060,000	2021	248,725,000	28,765,000	219,960,000
	2013	226,175,000	2028	204,575,000	11,625,000	192,950,000
	2015*	220,980,000	2026	220,980,000	0	220,980,000
			Total	2,498,895,000 *(FY 17 Debt)*	324,910,000 *(FY 17 Payment)*	2,173,985,000 *(FY 18 Debt)*

**refunding*

As shown in the table, Utah paid off the portion of Series 2010A bonds dedicated to capital facility projects and the Series 2004A bonds on July 1, 2016. The state will pay off the remaining outstanding capital facility projects bonds (Series 2011A and Series 2012A) and the highway projects portion of Series 2010A on July 1, 2017.

<u>Bond Defeasance</u>. Any bond can be legally defeased earlier than its final maturity date. Although a defeasance is generally accomplished by a refunding transaction, a defeasance can also occur with cash. Doing so involves setting aside sufficient cash or U.S. Treasury obligations in an escrow account to meet all principal and interest payments on the outstanding bonds as they become due until their call date, at which point the escrow retires the remainder of the debt. However, the interest rate in the escrow account cannot exceed the interest rate on the bonds ("arbitrage") or the bonds can lose their exemption from federal income tax. The last defeasance occurred in March 2015 and saved the state an estimated $10.4 million (net present value) when portions of Series 2009A and Series 2011A were refinanced.

<u>Build America Bonds Subsidy</u>. Utah issued five bond series using the federal Build America Bonds (BABs) program (two G.O. issues and three revenue bond issues) which used taxable bonds with a 35 percent direct cash subsidy paid by the U.S. Treasury to the issuer, rather than the traditional federally tax-exempt bond structure. The BABs program was originally projected to save the State approximately $55 million (net present value) over 15 years on $1.114 billion of G.O. bonds. Shortly after the program's inception, bond rating agencies recommended that BABs issuers budget debt service gross of federal subsidies, acknowledging the potential for Congress to curtail future subsidies. Correspondingly, the State appropriated an additional $14,139,000 from the General Fund to the Debt Service budget for FY 2016 and $14,214,000 for FY 2017. The funds will be transferred back to the General Fund upon receipt of the subsidy.

The potential for subsidies to be reduced was realized when the federal budget sequestration of 2013 reduced the FY 2014 subsidy payments by $1,098,200 or 7.2 percent of the original subsidy, thereby increasing the amount that had to be transferred from the TIF and County funds to cover the BABs shortfall. Future changes in subsidies will be determined by Congress as it sets appropriations under federal spending caps, meaning it is unclear whether additional sequestration which could affect BABs subsidies might occur. Unless sequestration-induced subsidy reductions are curtailed or otherwise changed, the projected savings realized through the use of BABs are now projected at approximately $44 million (net present value).

Constitutional and Statutory Bonding Capacity. The State's constitution caps total general obligation debt at 1.5 percent of the value of the taxable property in the state. The data that follow in this section are estimated as of April 5, 2016.

Fair market value of ad valorem taxable property	$292,490,917,013
Fees in lieu of ad valorem taxable property	$11,234,292,957
Total fair market value of taxable property	$303,725,209,970
Constitutional debt limit (1.5%)	$4,555,878,150
Less: currently outstanding general obligation debt (net)	($2,593,058,369)
Estimated additional constitutional debt incurring capacity of the State	$1,962,819,781
Currently outstanding G.O. debt as a percent of the constitutional debt limit	*56.9%*

The State's statutory debt limit caps general obligation debt at 45 percent of the maximum allowable appropriations limit unless approved by more than two-thirds of the Legislature. However, statute excludes most highway bonds from being subject to the statutory debt limitation. The State Appropriations and Tax Limitation Act and additional general obligation debt incurring capacity of the State under that act are estimated as of April 29, 2016 as follows:

Statutory general obligation debt limit	$1,563,488,550
Less: statutorily applicable general obligation debt (net)	($184,408,203)
Remaining statutory general obligation debt incurring capacity	$1,379,080,347

LEASE REVENUE (L.R.) BONDS

As shown in Table 3, the State's FY 2017 L.R. bond indebtedness is $315.65 million and the State will make FY 2017 principal payments totaling $23.05 million on May 15, 2017. Utah will pay off Series 2007A and Series 2009D on May 15, 2017.

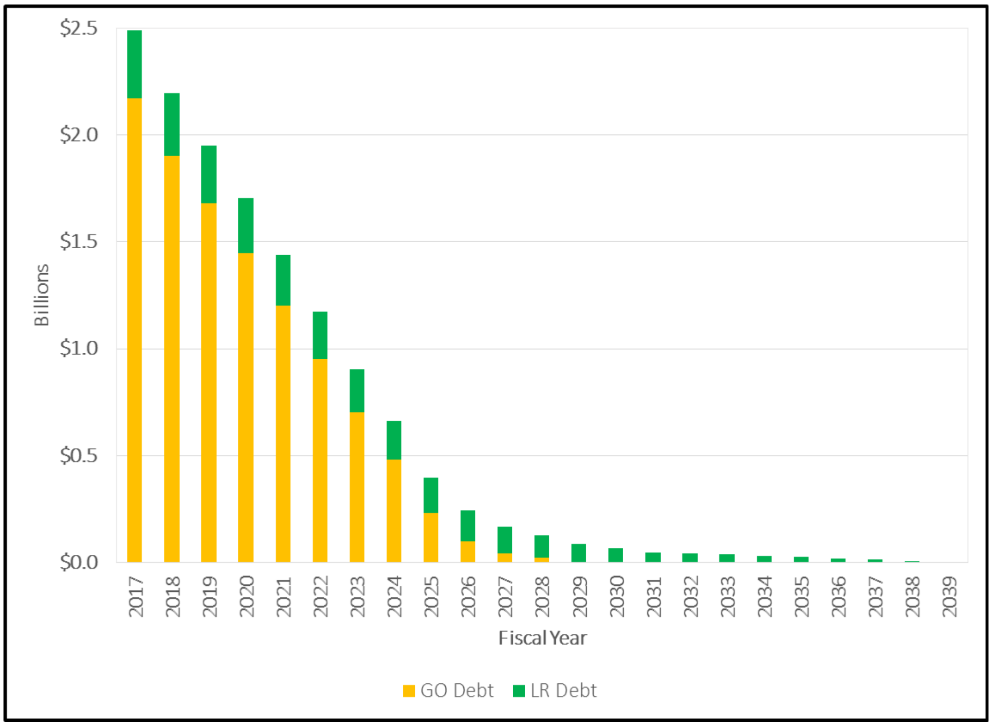
Table 3: Lease Revenue Bond Payments and Principal Outstanding

Series	Original Amount	Final Maturity Date May 15	July 1, 2016 Principal Outstanding	May 15, 2017 Principal Payment	July 1, 2017 Principal Outstanding
1998C	105,100,000	2019	19,535,000	9,130,000	10,405,000
2007A	15,380,000	2017	695,000	695,000	0
2009A	25,505,000	2019	3,225,000	1,025,000	2,200,000
2009B	8,445,000	2019	3,550,000	1,125,000	2,425,000
2009C	16,715,000	2029	16,715,000	0	16,715,000
2009D	12,125,000	2017	3,795,000	3,795,000	0
2009E	89,470,000	2030	89,470,000	0	89,470,000
2010	36,735,000	2024	25,580,000	3,175,000	22,405,000
2011	5,250,000	2031	3,560,000	385,000	3,175,000
2012A	15,610,000	2027	15,610,000	990,000	14,620,000
2012B	11,700,000	2022	6,555,000	2,380,000	4,175,000
2015	30,015,000	2030	29,210,000	350,000	28,860,000
2016	98,150,000	2038	98,150,000	0	98,150,000
		Total	315,650,000 *(FY 17 Debt)*	23,050,000 *(FY 17 Payment)*	292,600,000 *(FY 18 Debt)*

DEBT PAYOFF SCHEDULE

Chart 1 shows that under the current schedule (assuming no additional bonds issued), the State will make a final G.O. bond debt payment on the first day of FY 2029, and the State will have no G.O. bond debt by FY 2030; and the State will make a final L.R. bond debt payment in May 2038, and the State will have no L.R. bond debt by FY 2039.

Chart 1: General Obligation and Lease Revenue Bonds Principal Outstanding

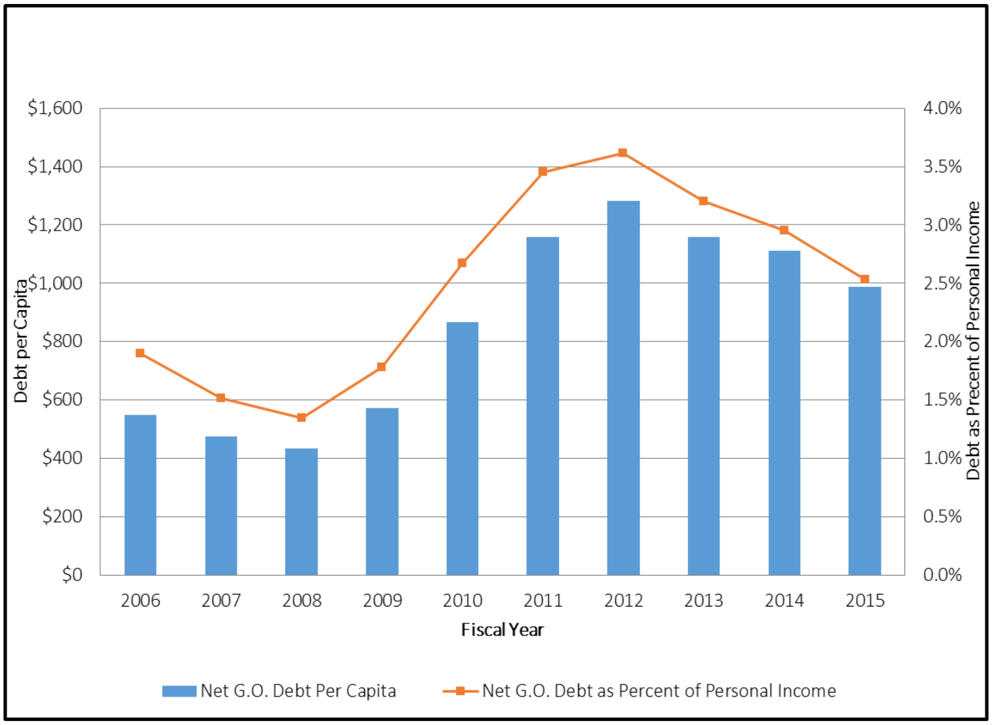


CREDIT RATING AND DEBT RATIOS

The three primary nationally recognized bond rating agencies, Moody's, Standard and Poor's, and Fitch, rate the general obligation debt of all states. As of April 2016, nine states merited the highest "Triple A" rating from all three agencies: Delaware, Georgia, Iowa, Maryland, Missouri, North Carolina, Texas, Utah, and Virginia.

Rating agencies and investors focus in particular on "debt affordability" measures, such as a state's outstanding debt relative to population and personal income. These indicators give insight into a state's indebtedness and the debt burden placed on taxpayers. Per capita debt is calculated by dividing the total outstanding debt by the current population estimate. Debt as a percent of personal income is calculated by dividing current outstanding debt by the state's total personal income. Chart 2 shows a history of Utah's G.O. debt affordability as measured by these two ratios.

Chart 2: Net G.O. Debt Per Capita and as a Percent of Personal Income



Utah's FY 2015 net G.O. debt per capita was $988 while the State's debt as a percent of personal income was 2.53 percent. Both measures have declined from their peaks in FY 2012, which resulted from increased bonding for highway projects including the reconstruction of I-15 in Utah County and the Critical Highway Needs program; and both are more than double their 10-year lows that occurred in FY 2008, just prior to the Great Recession.

Among the nine Triple A states, Utah ranks near the middle on several measures of debt affordability. As reported by Moody's Investor Service, Chart 3 shows net tax-supported debt (NTSD) per capita and NTSD as a percent of personal income, and Chart 4 shows NTSD as a percent of state gross domestic product along with each state's debt service ratio. In order to increase its attractiveness to investors, Utah should continue to strive to improve its standing in debt affordability measures relative to other Triple A states.

Chart 3: NTSD Per Capita and NTSD as a Percent of 2014 Personal Income

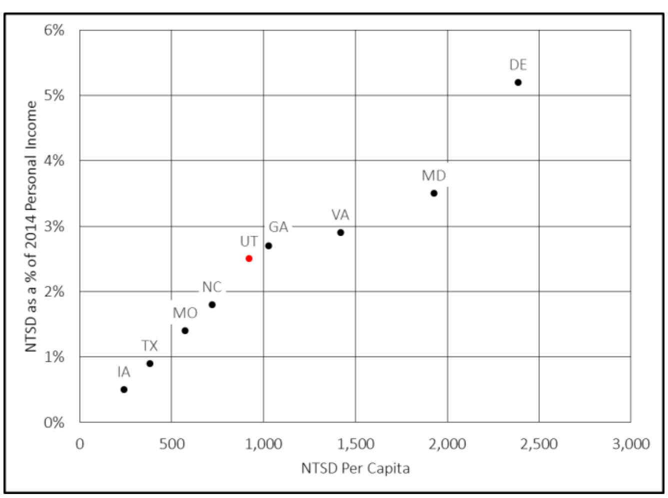


Chart 4: NTSD as a Percent of State Gross Domestic Product and Debt Service Ratio