DEBT SERVICE OVERVIEW

INFRASTRUCTURE AND GENERAL GOVERNMENT APPROPRIATIONS SUBCOMMITTEE
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ISSUE BRIEF

OVERVIEW

In July 2017, the State closed on General Obligation Bonds, Series 2017 that generated proceeds of $120.0 million for the prison project and $46.9 million for transportation projects. The bonds sold at a true interest rate of 1.8 percent and the final debt payments will occur on July 1 of 2027 and 2032 for the prison portion and transportation portion, respectively. The State plans to issue additional bonds over the next three years that will generate proceeds of approximately $450.0 million for the prison project, and over the next four years that will generate proceeds of approximately $1.0 billion for transportation projects.

The State's general obligation (G.O.) bond debt reached a peak of about $3.7 billion in FY 2012, and it declined steadily to about $2.1 billion by July 2017 (including debt incurred with issuance of Series 2017). With the additional issuances described above, debt is projected to peak at about $2.8 billion in FY 2020. Debt service, the amount required to make principal and interest payments, fluctuated between about $407 million and $455 million from FY 2012 through FY 2017. The Legislature shifted about $70 million of appropriations that had been going to debt service to capital development for FY 2018 and FY 2019, and it directed that the funds revert to debt service beginning in FY 2020. Debt service from FY 2020 through FY 2025 is projected to range between $405 million and $450 million, and then to decline steadily as bonds are paid off.

DEBT SERVICE BUDGET

Debt service constitutes payment of interest and principal 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 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 lease revenue bonds. As shown in Table 1 below, beginning with FY 2018 the use of funds for G.O. bond debt service is tracked separately for higher education, public education, transportation, and other state government.

The state paid $466.4 million for debt service in FY 2016 and the Legislature appropriated $458.9 million in FY 2017 and $381.1 million in FY 2018 for debt service. Table 1 shows sources of finance and use of funds for debt service for FY 2016 actual, FY 2017 revised appropriated, and FY 2018 appropriated (https://le.utah.gov/lfa/cobi/currentCobi/cobi.html?cobiID=637&tab=financialsTab).

Table 1: Debt Service Sources of Finance and Uses of Funds

Source of Finance	FY 16 Actual*	FY 17 Rev. App.	FY 18 Appropriated
General Fund	54,535,800	54,535,800	8,535,800
Gen. Fund, One-time	14,139,000	14,200,000	49,716,500
Education Fund	17,221,800	17,221,800	17,221,800
Edu. Fund, One-time			(3,942,100)
TIF of 2005	348,420,200	348,420,200	275,181,800
TIF of 2005, One-time		(22,957,700)	
Federal Funds	15,843,900	15,758,900	15,827,000
Federal Funds, One-time		68,100	
Ded. Credits Revenue	23,994,500	27,357,300	24,959,400
County of 1st Class	6,383,600	7,409,500	7,835,900
Transfers	(13,922,200)	(14,200,000)	(14,200,000)
Beginning Nonlapsing	8,657,000	19,023,300	7,931,500
Closing Nonlapsing	(8,844,900)	(7,931,500)	(7,931,500)
Use of Funds			
G.O.	440,601,100	418,716,300	
G.O. – Higher Education			36,866,500
G.O. – Public Education			
G.O. – Transportation			297,217,700
G.O. – State Government			20,242,500
L.R.	25,827,600	40,189,400	26,809,400
Total	*466,428,700*	*458,905,700*	*381,136,100*

* FY 2016 actuals are rounded to the nearest hundred.

GENERAL OBLIGATION (G.O.) BONDS

Outstanding G.O. Bonds. The State's G.O. bond indebtedness as of July 10, 2017 was $2.13 billion as reported in the Official Statement for the State of Utah General Obligation Bonds, Series 2017 (2017 O.S.) (p. 13). The debt included $142.1 million of bonds issued in July 2017 (p. 13) to fund construction of the prison and transportation projects and $86.4 million in total unamortized bond premium (p. 14). It did not include approximately $1.52 billion in bonds authorized by the Legislature but not yet issued for these purposes (p. 13). Table 2 shows G.O. bond principal outstanding broken out by prison and highway projects and total unamortized bond premium (p. 14, Zions Public Finance Inc, and Division of Finance).

Table 2: General Obligation Bonds Principal Outstanding

	Series	Original Principal Amount	Final Maturity Date July 1	Principal Outstanding as of July 10, 2017
Prison	2017	100,810,000	2027	100,810,000
Highway Projects	2009A	394,360,000	2018	25,265,000
	2009C**	363,630,000	2018	70,865,000
	2009D	491,760,000	2024	491,760,000
	2010B	621,980,000	2025	621,980,000
	2010C*	172,055,000	2019	114,910,000
	2011A**	563,060,000	2021	175,965,000
	2013	226,175,000	2028	180,725,000
	2015*	220,980,000	2026	220,980,000
	2017	41,260,000	2032	41,260,000
			Total Unamortized Premium	86,403,000
			Total	2,130,923,000

* refunding
** the series included funds for highways (shown in the table) and for buildings (paid off)

Bond Defeasance. Any bond can be legally defeased earlier than its final maturity date. Although a defeasance is generally accomplished by a refunding (refinancing) transaction, a defeasance can also occur with cash. Doing so involves setting aside sufficient cash or U.S. government 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, there are limits to the degree which interest rates in escrow can exceed interest rates on the bonds (creating "arbitrage"), such that the bonds could lose their federally tax-exempt status. 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.

Build America Bonds Subsidy. 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, in lieu of 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 approximately $1.11 billion of G.O. bonds. However, the United States Congress has reduced subsidies and the actual savings realized will be slightly less than the amount originally projected. The state budgets for debt service gross of federal subsidies to ensure sufficient funds to make payments regardless of federal actions – the State appropriated an additional $14,200,000 from the General Fund to the Debt Service budget for FY 2017 and for FY 2018, and the funds will be transferred back to the General Fund upon receipt of the federal subsidy.

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 July 10, 2017 as reported in the 2017 O.S. (p. 11).

Fair market value of ad valorem taxable property	$311,651,315,372
Fees in lieu of ad valorem taxable property	$11,715,772,601
Total fair market value of taxable property	$323,367,087,973
Constitutional debt limit (1.5%)	$4,850,506,320
Less: currently outstanding general obligation debt (net)	($2,130,923,004)
Less: long-term contract liabilities*	($87,846,000)
Estimated additional constitutional debt incurring capacity of the State	$2,631,737,316

The State's outstanding G.O. debt and long-term liabilities as a percent of the constitutional debt limit is about 45.7 percent.

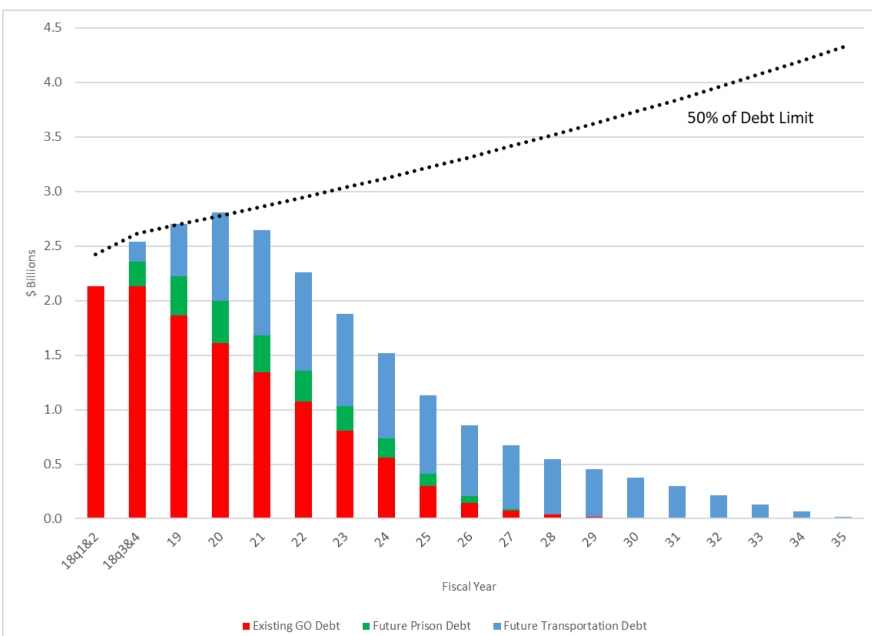
The State's statutory debt limit caps general obligation debt at 45 percent of the maximum allowable appropriations limit unless approved by more than two-thirds of the Legislature. However, statute excludes most highway bonds from being subject to the statutory debt limitation. Based on the State Appropriations and Tax Limitation Act, additional general obligation debt incurring capacity of the State under that act is estimated as of July 10, 2017 as follows (2017 O.S., p. 12):

Statutory general obligation debt limit	$1,617,538,229
Less: statutorily applicable general obligation debt (net)	($120,448,580)
Less: long-term contract liabilities*	($87,846,000)
Remaining statutory general obligation debt incurring capacity	$1,409,243,649

* In the opinion of the State Auditor, the State has long–term contract liabilities consisting of unused vacation, notes payable, and certain settlement amounts and other vested leave for employees of approximately $87,846,000 which financial obligations may be considered as general obligation debt of the State. There has not been a final legal determination on this opinion.

G.O. Debt Issuance and Payoff Schedule. Chart 1 depicts existing G.O. bond debt and models future issuance of authorized but not yet issued prison and transportation debt. Under this scenario, the State will make a final G.O. debt payment on July 1, 2035.

Chart 1: Existing and Future General Obligation Bond Debt



LEASE REVENUE (L.R.) BONDS

As shown in Table 3, the State Building Ownership Authority's outstanding principal for L.R. bonds was $292.6 million as of July 10, 2017 (2017 O.S., p. B-2). Under the current schedule (assuming no additional bonds issued), the State will make a final L.R. bond debt payment on May 15, 2038.

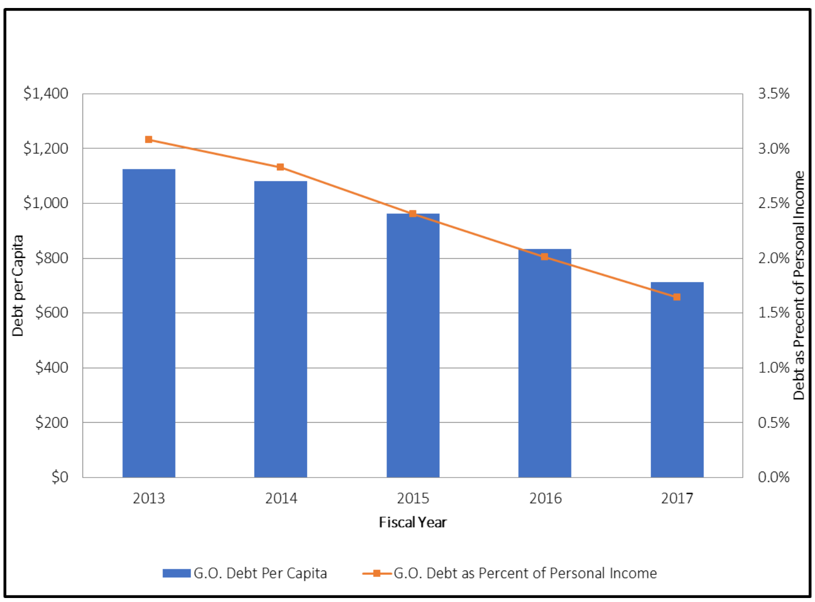
Table 3: Lease Revenue Bonds Principal Outstanding

Series	Original Amount	Final Maturity Date May 15	Principal Outstanding as of July 10, 2017
1998C	105,100,000	2019	10,405,000
2009A	25,505,000	2019	2,200,000
2009B	8,445,000	2019	2,425,000
2009C	16,715,000	2029	16,715,000
2009E	89,470,000	2030	89,470,000
2010	36,735,000	2024	22,405,000
2011	5,250,000	2031	3,175,000
2012A	15,610,000	2027	14,620,000
2012B	11,700,000	2022	4,175,000
2015	30,015,000	2030	28,860,000
2016	98,150,000	2038	98,150,000
		Total	292,600,000

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. Utah is one of eight states that currently receives the highest "Triple A" rating from all three agencies. When evaluating a state's debt, rating agencies and investors focus in particular on "debt affordability" measures, such as a state's outstanding debt relative to population and personal income. Chart 2 shows Utah's G.O. debt affordability as measured by these two ratios for the past five fiscal years as reported in the 2017 O.S. (p. 17).

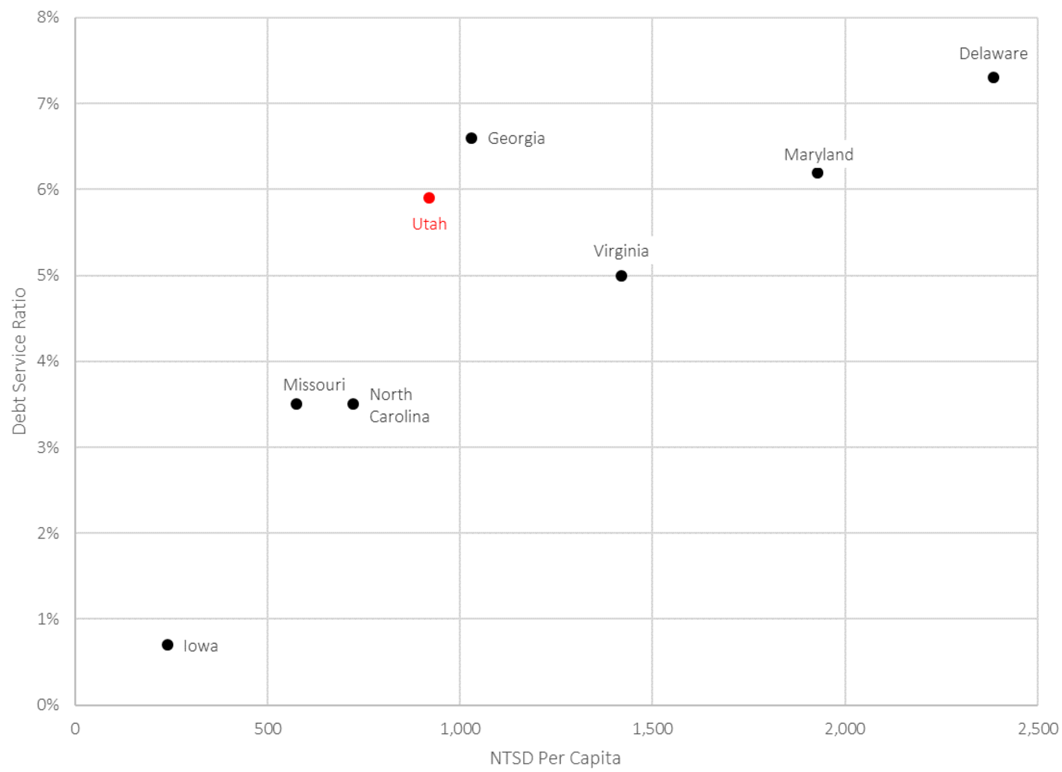
Chart 2: G.O. Debt Per Capita and as a Percent of Personal Income



Utah's FY 2017 G.O. debt per capita was $712 and its debt as a percent of personal income was 1.64 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. However, both measures will rise as the State issues additional debt that has been already been authorized for prison construction and transportation projects.

As shown in Chart 3, Utah ranked near the middle among the eight current consensus Triple-A states on the following measures of debt affordability*: net tax-supported debt (NTSD) per capita and debt service as a ratio of state revenue.

Chart 3: NTSD Per Capita and NTSD and Debt Service Ratio



* Data was reported by Moody's Investor Service for 2014 – the most recent data available to the fiscal analyst.