**Legislative Fiscal Bureau**

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: http://legis.wisconsin.gov/lfb

May 10, 2016

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Deferral of Principal Payment of Commercial Paper

Recently, the Department of Administration informed this office of their decision to defer a payment of $50 million in GPR-supported, commercial paper principal that was scheduled to be repaid on May 1, 2016. In addition, the administration informed us that $50 million, plus interest, would be paid over an eight-year period from 2016-17 to 2023-24 ($6,250,000 plus interest annually).

Based upon that information, we prepared the attached memorandum for distribution to the members of the Joint Committee on Finance.

Subsequent to the distribution of the attached document, the administration informed us that rather than deferring principal payment on $50 million, they now intend to defer payment on $101 million.

Assuming that the deferral will occur in 2015-16 and that payment of the $101 million will be reamortized over an eight-year period, the following table indicates the repayment schedule from 2016-17 to 2023-24.

**Expected Repayment Schedule on $101 Million in Commercial Paper Principal Deferred in May, 2016**

| | Principal | Interest | Total Debt Service | Outstanding Principal |
|---|---|---|---|---|
| 2016-17 | $12,625,000 | $505,000 | $13,130,000 | $88,375,000 |
| 2017-18 | 12,625,000 | 441,875 | 13,066,875 | 75,750,000 |
| 2018-19 | 12,625,000 | 378,750 | 13,003,750 | 63,125,000 |
| 2019-20 | 12,625,000 | 315,625 | 12,940,625 | 50,500,000 |
| 2020-21 | 12,625,000 | 252,500 | 12,877,500 | 37,875,000 |
| 2021-22 | 12,625,000 | 189,375 | 12,814,375 | 25,250,000 |
| 2022-23 | 12,625,000 | 126,250 | 12,751,250 | 12,625,000 |
| 2023-24 | 12,625,000 | 63,125 | 12,688,125 | - |
| Total | $101,000,000 | $2,272,500 | $103,272,500 | |

Attachment

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May 10, 2016

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Deferral of Payment of GPR-Supported Commercial Paper Principal

This memorandum provides information on the administration's decision to defer the payment of $50 million in GPR-supported, commercial paper principal that was scheduled to be repaid on May 1, 2016.

**Background**

The Building Commission has authorized a general obligation commercial paper and general obligation extendible municipal commercial paper financing programs. The programs involve the state issuing short-term commercial paper notes with maturities of 270 days or less in order to delay the issuance of long-term bonds for a period. The programs try to take advantage of short term borrowing rates, when those rates are substantially lower than long term rates.

The state's long-term general obligation debt principal is typically amortized over a 10- or 20-year period depending on the life of the asset being financed by the bond proceeds. The Building Commission and the Department of Administration (DOA), as matter of practice, have typically required that the state's general obligation commercial paper programs amortize the repayment of principal over the life of the asset being financed, which is similar to how the state retires its long-term general obligation debt. These principal repayments on the state's general obligation short-term borrowing programs are then included in the annual budgeted debt service amounts and paid from the same debt service appropriations as the state's long term debt. However, no statutory requirement exists that DOA retire the state's short-term debt obligation principal in this manner. Rather, only the lower short-term interest accruing annually on the commercial paper obligations are technically required to be paid.

**Debt Refinancing**

Generally, the state's debt is refinanced in either an economic refunding or a structural refunding, or a combination of those methods. In an economic refunding, the new stream of debt service payments is designed to reduce the total cost of the outstanding debt and is typically undertaken to take advantage of reduced interest rates. No increase in debt service payments occurs in any year due to an economic refunding and debt service payments are reduced in some or all years during the life of the refunding issue. The transaction can be structured so that the debt service savings are realized equally in each year during the life of the refunding bonds or concentrated in the early or late years of the transaction.

In a structural refunding, the new stream of debt service payments can be higher or lower in a given year than under the current stream of payments. For example, the debt service payments in the early years of the refunding could be reduced while debt service payments are increased in future years. A structural refunding tends to increase the average life of debt. Bonds are outstanding longer and therefore, the interest costs tend to be greater.

Since 2001, the state has carried out the structural refunding of $1,563.1 million in short-term commercial paper and general obligation bond principal payments through the issuance of refunding bonds. Under these structural refunding actions, the state issued refunding bonds and used the proceeds on those bonds to make payments on current year principal due on its general obligation debt, or rolled over commercial paper principal that otherwise would have been paid off. These actions increased the average life of the debt refunded, and because the principal that would have been repaid was outstanding longer, the state incurred higher interest costs. The structural refunding of long-term debt was authorized by the Legislature.

Unlike the economic or structural refinancing of long-term general obligation debt, the administration can restructure the repayment of principal under the commercial paper programs without legislative approval. In order to reduce current year GPR expenditures administrations have chosen not to repay the principal portion of commercial paper debt that had previously been scheduled to be repaid and that was budgeted for by the Legislature.

**May, 2016 Commercial Paper Principal Payment**

The state had approximately $131.7 million in commercial paper principal that was scheduled to be retired on May 1, 2016, and budgeted for under the 2015-17 biennial budget. A large percentage of this principal is scheduled to be repaid from GPR appropriations. The administration has indicated that it has deferred $50 million of the GPR commercial paper principal scheduled to be repaid on May 1, 2016, which will reduce GPR debt service costs by $50 million in 2015-16. This will increase the 2015-16 general fund ending balance by $50 million compared to previous estimates.

DOA Capital Finance officials indicate that the $50 million in commercial paper principal will be reammortized over an eight-year period, beginning with 2016-17. As indicated in the following table, because this principal will be outstanding longer, the state will incur an estimated $1,125,000 in additional interest costs associated with this $50 million in commercial paper general obligation debt, assuming an annual interest rate of 0.5%. The following table indicates the principal repayment schedule along with the estimated interest costs associated with the administration's decision to defer the repayment of $50 million in commercial paper principal due on May 1, 2016.

**Expected Repayment Schedule on $50 Million in Commercial Paper Principal Deferred in May, 2016**

| | Principal | Estimated Interest | Total Debt Service | Outstanding Principal |
|---|---|---|---|---|
| 2016-17 | $6,250,000 | $250,000 | $6,500,000 | $43,750,000 |
| 2017-18 | 6,250,000 | 218,750 | 6,468,750 | 37,500,000 |
| 2018-19 | 6,250,000 | 187,500 | 6,437,500 | 31,250,000 |
| 2019-20 | 6,250,000 | 156,250 | 6,406,250 | 25,000,000 |
| 2020-21 | 6,250,000 | 125,000 | 6,375,000 | 18,750,000 |
| 2021-22 | 6,250,000 | 93,750 | 6,343,750 | 12,500,000 |
| 2022-23 | 6,250,000 | 62,500 | 6,312,500 | 6,250,000 |
| 2023-24 | 6,250,000 | 31,250 | 6,281,250 | - |
| Total | $50,000,000 | $1,125,000 | $51,125,000 | |

The estimated reduction in principal payments in 2015-16 and the increase in principal and interest payments in 2016-17 will be incorporated in the final Chapter 20 schedule of appropriations that will be printed in the statutes, after approval by the Committee.

BL/AR/SAS