Legislative Fiscal Bureau

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GPR Supported Debt and Bonding Overview (Building Program)

[[LFB 2011-13 Budget Summary: Page 552, #1]

This paper discusses the use of bonding by the state and the existing level of state general obligation bonding debt. Specifically, the paper deals with the amount of GPR supported general obligation bonds. In addition, information is provided on the amount of existing GPR supported bonding that may be issued in the 2011-13 biennium, as well as the amount of GPR supported bonding included under Assembly Bill 40 (AB 40) and under the Building Commission's 2011-13 biennial state building program recommendations. Finally, the paper discusses the amount of GPR supported debt service that will repaid in the 2011-13 biennium and into the future.

Use of Bonding to Finance Projects and Programs

In April, 1969, voters approved an amendment to the Wisconsin Constitution authorizing the state to issue debt directly. The amendment enabled the state to "acquire, construct, develop, extend, enlarge or improve land, waters, property, highways, buildings, equipment or facilities for public purposes." The language was deliberately broad, requiring only that bonding be intended to affect physical property directly and be undertaken for public purposes. In April, 1975, another constitutional amendment was passed, specifically permitting the state to issue general obligation bonds for veterans' housing loans. In April, 1992, a further constitutional amendment authorized the use of general obligation bonds for railways.

State governments have financed their capital project and programmatic requirements using three options: paying for projects with cash, borrowing for projects and repaying the resulting debt over time, and leasing facilities. The specific purposes for which general obligation debt may be contracted are authorized by the Legislature. Most of these bonding authorizations are contained in the biennial budget to fund that biennium’s building program, as well as other bonding programs. The Building Commission, with the assistance of the Department of Administration's capital finance office then issues the bonds to fund the projects or program purposes for which the bonding was authorized.

Using cash requires the appropriation of either lump sum amounts, usually for smaller projects, or a series of amounts as larger facilities are built over several years. An advantage of using cash is that it may cost less, since there are no interest or debt issuance costs. A disadvantage is that adverse fiscal conditions or competing spending priorities can result in insufficient revenues to fund projects. If state revenues run low, new capital projects may be delayed or dropped. Alternatively, using cash could require a tax increase to fund government financing requirements, which can be politically difficult.

If current revenues cannot support state capital improvement needs, states may choose bonding to finance the projects. Long-term borrowing for capital construction has several advantages: (a) costs can be spread over the useful life of projects, with future users of projects sharing those costs; (b) citizens can derive near-term benefits from capital expenditures; (c) higher taxes to provide necessary capital facilities may be avoided; and (d) costs may be reduced in periods of high inflation when the interest paid on debt is less than the increased construction costs from waiting to finance projects with cash.

State GPR Supported General Obligation Debt

The state's outstanding debt represents the principal amount of debt that remains to be repaid on the total amount of general obligation bonds issued at that point in time. For example, as of December, 2010, Wisconsin had approximately $6.8 billion of general obligation bonds and commercial paper obligations outstanding, which represents the principal amount of debt that remained to be paid from issuing approximately $19.0 billion of general obligation bonds and commercial paper to that date. Table 1 presents a summary of the outstanding state general obligation indebtedness as of December, 2010.

TABLE 1

Outstanding General Obligation Debt -- As of December, 2010

Bonding Category	Amount Outstanding
Tax Supported	
General Fund	$4,654,153,581
Segregated Funds	664,937,902
Subtotal	$5,319,091,483
Self-Amortizing	
Veterans' Mortgage Loans	$222,745,000
University of Wisconsin And Other Categories	1,280,935,498
Subtotal	$1,503,680,498
Total	$6,822,771,981

As shown in Table 1, outstanding GPR supported debt, the focus of this paper, made up $4.65 billion, or 68.2%, of the state's $6.8 billion in outstanding general obligation debt. The level of state indebtedness has grown over time, which occurs because the amount of new debt that has been issued has exceeded the principal amount of debt repaid. Table 2 indicates the growth in GPR supported debt since 2000.

TABLE 2

Outstanding GPR Supported Debt
($ in Millions)

Year	Debt Outstanding	Annual Percent Change	Cumulative Percent Change
2001	$2,985.9		
2002	3,121.6	4.5%	4.5%
2003	3,138.3	0.5	5.1
2004	3,225.3	2.8	8.0
2005	3,856.3	19.6	29.2
2006	4,080.5	5.8	36.7
2007	4,064.5	-0.4	36.1
2008	4,154.5	2.2	39.1
2009	4,302.6	3.6	44.1
2010	4,654.2	8.2	55.9

Additional GPR Supported Debt Available in 2011-13

The additional amount of GPR supported debt that would be available in the biennium would be the sum of the following: (a) newly authorized bonding included in the 2011-13 state building program; (b) program-related and other bonding amounts included in AB 40, the biennial budget bill; and (c) previously authorized bonding amounts that are not available for issue until the 2011-13 biennium.

As part of the biennial building program, the Legislature also authorizes any new bonding or other monies needed to fund the projects enumerated in the state building program. The Building Commission's 2011-13 building program recommendations include the authorization of $735.8 million in new general obligation bonding, of which $424.3 million would be GPR supported bonding. In addition, the Commission also recommends a reduction of $8.7 million in GPR bonding for projects enumerated as part of previous state building programs for a net increase of $415.6 million. Table 3 indicates how the $415.6 million in GPR supported bonding authorizations under the Building Commission's recommendations for the state building program compares with past biennial building programs. However, of this amount, only $277.7 million would be available in the 2011-13 biennium.

TABLE 3

GPR Supported General Obligation Bonding
Authorized in Biennial State Building Programs*
($ in Millions)

Biennium	Authorization
1995-97	$246.7
1997-99	366.2
1999-01	425.4
2001-03	709.8
2003-05	247.2
2005-07	499.1
2007-09	412.3
2009-11	522.4
2011-13	415.6

*Amounts shown include bonding amounts authorized in each biennium rather than the biennium in which the bonding becomes available for issue.

In addition to the GPR supported bonding being recommended by the Building Commission to fund 2011-13 state building program projects, the Governor's biennial budget recommendation also includes bonding authorizations for other program purposes. AB 40 would authorize $128.8 million in GPR supported bonding for the following non-building program purposes, which would be available in the 2011-13 biennium: (a) $9.4 million for the environmental improvement fund's safe drinking water program; (b) $4.0 million in DNR's dam safety projects funding; and (c) $115.4 million in the Department of Transportation state rehabilitation projects funding. AB 40 would reduce the amounts of previously authorized, but not yet issued, GPR supported bonding by $112.0 million associated with the deletion of the southeast Wisconsin transit capital assistance program ($100 million) and a reduction in the DATCP's agricultural conservation easements program funding ($12 million). In an earlier action, the Committee added $6.7 million in GPR supported bonding for the environmental improvement fund's clean water fund improvement program. Therefore the net increase in program-related bonding in AB 40 would be $23.5 million.

GPR supported bonding authorized under previous building programs and for program purposes, such as the state's stewardship program also would become available for issuance during the 2011-13 biennium. The 2009-11 state building program authorized four UW System projects funded with $199.9 million in GPR supported bonding that could not be issued until the 2011-13 biennium (this amount excludes the $13 million in GPR supported bonding for a Department of Military Affairs armory facility Wisconsin Rapids that is being amended as part of the 2011-13 state building program recommendations). In addition, $120 million in previously authorized GPR supported bonding for the state's stewardship program would become available for issue in the 2011-13 biennium (this amount reflects the Committee's earlier action to reduce the annual stewardship borrowing from $86 million to $60 million). Table 4 identifies the GPR supported debt that could be issued in the 2011-13 biennium under AB 40, the Building Commission's recommended 2011-13 state building program, and the existing bonding authorizations that become available for issue in the biennium.

TABLE 4

Additional GPR Supported Bonding Available For Issue in the 2011-13 Biennium ($ in Millions)

	Amount
2011-13 Building Program Bonding Issued in Biennium	$277.7
Bonding under AB 40	
Net Increase in Program-Related Bonding	23.5
Existing Bonding Available in 2009-11 Biennium	
Previously Enumerated Projects	199.9
Stewardship Program	120.0
Total	$621.1

As indicated in Table 4, under current law, AB 40, and the 2011-13 state building program recommendations, an estimated $621.1 million in GPR supported bonding would be available for issuance in the biennium, or approximately $310.6 million per year. For comparison, over the past 10 years, the state has issued an estimated average of $404.0 million in GPR supported bonding each year. Given this history, the amount of additional GPR supported bonding available in the biennium would be less than the average level of issuance in recent years.

The state Constitution imposes a ceiling on the aggregate amount of general obligation debt the state may incur in any calendar year. Over the past 10 years, the state has ranged between 12.8% and 25.3% of this annual limit. In addition, there is an alternative calculation of the annual debt limit under the Constitution that is based on the cumulative level of outstanding debt. Under this calculation, the state has used 26.1% of the allowable net indebtedness. Therefore, the state's annual debt issuance has been well under the limits on debt issuance established in the Constitution. Given the proposed level of GPR supported bonding that would be available in the biennium, the state will likely remain well below the constitutional debt limits.

GPR Debt Restructuring

In recent biennia, due to budgetary constraints on the state's general fund, the state has deferred paying a portion of the GPR principal on its outstanding GPR supported debt. These actions have the effect of lowering the amount of GPR debt service paid in a specific year. However, debt service costs in subsequent years are higher than they otherwise would be because these "rolled over" principal amounts are again scheduled to be repaid. Also, until these principal amounts are repaid, the state's incurs additional interest on these unpaid amounts.

AB 40 would continue the state's debt restructuring trend. The Governor's budget proposes issuing an additional $437.4 million in GPR supported debt in order to restructure the same amount of GPR principal payments due on the state's outstanding GPR supported debt in 2011-12, which would be the largest, annual amount of debt restructuring to date [see LFB Paper #175 for a discussion of the Governor's debt restructuring proposal].

Debt Service on GPR Supported Bonding

Historically, the state's debt management has been geared toward maintaining annual GPR debt service at no more than 4.0% of annual GPR tax revenues, with a target of annual GPR debt service that is between 3.0% and 3.5% of annual GPR tax revenues. This policy is intended to ensure that debt service does not consume an increasing share of the state budget and add to state out-year spending commitments. In developing its building program recommendations, the Building Commission considers the impact bonding authorizations would have on the GPR debt service to GPR revenues ratio. However, this impact is not a good measure for determining the amount of bonding to recommend in a biennial building program, because much of the bonding authorized in one biennium will not fully impact state GPR debt service payments until the following biennium at the earliest. For example, the full debt service impact of any bonds issued as result of the Building Commission's 2011-13 building program recommendations would not fully affect the GPR debt service to revenue ratio until the 2013-15 biennium at the earliest.

Estimates of future debt service amounts contain three primary components: (a) existing debt service on bonds that have been issued; (b) estimated debt service on bonds that have been previously authorized, but not yet issued; and (c) estimates on debt service for bonds authorized in the current biennium. Bonds are not always issued in the biennium in which the bonds are authorized, due to the timing of projects, or the bonds were authorized for a multi-year purpose like the state's stewardship program. These increased debt service amounts will be partially offset by old debt being retired during the period the bonds remain outstanding.

Table 6 provides an estimate of GPR debt service through the 2013-15 biennium based on the amount of existing debt, an estimate of the amounts of currently authorized debt that may be issued, and the anticipated issuance of the bonding proposed under AB 40 and the 2011-13 state building program. The table also indicates the debt service reductions in the current year and in the 2011-12, and the increases in expected debt service in future years, associated with the past deferral of GPR principal amounts and the amounts proposed under AB 40. As indicated in the table, the GPR bonding amounts in the bill and those amounts recommended in the 2011-13 building program would not impact GPR debt service amounts significantly until the 2013-15 biennium.

TABLE 6

Comparison of Estimated GPR Debt Service with Hypothetical GPR Tax Revenues
($ in Millions)

	2011-12	2012-13	2013-14	2014-15
Existing debt service*	$639.7	$633.5	$610.6	$546.2
GPR debt service on unissued authorized bonding	3.3	24.7	39.0	47.6
GPR debt service on deferred principal**	-431.5	19.4	74.5	74.5
GPR debt service on 2011-13 authorized bonding	0.0	5.1	23.4	43.3
Total	$211.5	$682.7	$747.5	$711.6
GPR tax revenues estimates	$13,368.4	$13,888.0		
at 2% growth			$14,165.8	$14,449.1
at 3% growth			14,304.6	14,733.8
at 4% growth			14,443.5	15,021.3
GPR debt service as percent of GPR tax revenues	1.58%	4.91%		
at 2% growth			5.28%	4.92%
at 3% growth			5.23	4.83
at 4% growth			5.18	4.74

* Includes offsets to GPR debt service with other sources.

** This amount was $437.4 million under AB 40. However a $5.9 million 2012 bond maturity was refinanced as part of the Spring, 2011, debt restructuring transaction, which lowered the existing debt service for 2011-12 by that same principal amount.

As indicated in Table 6, the ratio of GPR debt service to GPR revenues is estimated to increase from a range of just over 4.7% to nearly 5.3%, under the illustrated levels of growth in revenues, which is well above the state's 3.0% to 4.0% target. The growth in this ratio is due primarily to the restructured GPR principal amounts that have been deferred in recent years having to be repaid and to the higher levels of GPR bonding authorized in recent biennia.

Another measure of the impact that additional GPR borrowing is how would the additional borrowing impact the state's GPR debt level. Under this measure, if the state pays off more GPR principal on its debt than the amount of new debt issued, the state's GPR debt level would go down. This has not occurred since 2007. Under current law, the state is scheduled to retire $437.4 million in GPR principal in 2011-12 and $423.5 million in GPR principal in 2012-13. However, as mentioned earlier, the $437.4 million in 2011-12 would be restructured under the Governor's budget. As a result, under AB 40, the state would only pay off the $423.5 million in GPR principal due in the biennium. Given the level of existing GPR bonding available in the biennium, as well as the amounts recommended in AB 40 and the 2011-13 state building program, it is likely the level of GPR supported bonding issued in the biennium would exceed the $423.5 million in debt to be repaid. As a result, under AB 40, the state's GPR debt level will continue increase to increase through the 2011-13 biennium.

State Bond Ratings

In general, the bond market, by assessing the state's ability to meet its debt service obligations, along with its programmatic and administrative governmental functions, provides an indicator of the cumulative debt levels of the state. Wisconsin's bond issuance and debt service levels are considered in the high-moderate range by rating agencies. Rating agencies have generally cited concerns about the state's finances in their ratings of the state general obligation debt. Specifically, they have identified the state's lack of general fund surpluses, the lack of a significant reserve or "rainy day" fund, and the use one-time revenues to fund ongoing expenditures as credit concerns. These factors have contributed to the state's ongoing accounting deficit under generally accepted accounting principles (GAAP). The GAAP deficit generally reflects the state's year end general fund balance under its statutory basis of accounting adjusted for revenue and expenditure items attributable to the current fiscal year, which is exacerbated when annual general fund surpluses are low, or do not exist. For example, in 2009-10, while the state had a positive balance of $149.5 million using the statutory basis of accounting, when presented using GAAP, the state had a GAAP deficit of $2.9 billion.

As shown by the state's recent pattern of having to defer principal payments on its debt, the state is having difficulty funding its ongoing costs, let alone accumulating any significant general fund reserves. If bonding rating agencies determine that the state's debt levels are increasing faster than the state's relative ability to repay that debt, the state could have to pay higher interest rates and eventually the state's bond rating could suffer. However, due to current low market interest rates, the state's rating has not yet significantly impacted the state's cost of borrowing.

Summary

Determining the level of new GPR supported bonding in a biennium involves taking into account several issues. Those who place more concern on the state's increasing GPR supported debt contend that the state should limit the level of new, GPR supported bonding authorized in the biennium so as not to add to the state GPR debt level. They would note that GPR debt levels have risen in recent years faster than the state's ability to make the GPR debt service payments, as evidenced by the recurring levels of debt restructuring over the past ten years. Others who give more weight to the use of debt as a means to assist the state through periods when the state's general fund budget is stressed, may contend that additional GPR borrowing and debt restructuring is warranted in order to maintain vital program priorities and provide a boost to the state's economy during tough economic times.

If the Committee is concerned about the about the rising level of the state's GPR supported debt, as well as, the state's ability to repay that debt in future, the Committee could: (a) reduce the amount of GPR debt restructuring (See LFB Paper #175 for alternatives); (b) reduce the amount of existing bonding (which the Committee has already done with regard to the stewardship program -- also see LFB Paper #181 on authorized unissued PR supported bonding); (c) reduce the amount of program bonding included under AB 40, which would most likely mean a reduction in GPR supported bonding for highway rehabilitation; or (d) reduce the GPR supported bonding included in the 2011-13 state building program.

The Committee has yet to act on the Governor's debt restructuring proposal in the budget bill. The GPR debt restructuring proposal would essentially fund the gap between GPR revenues in 2011-12 and GPR program costs in that year under the Governor's bill. The Committee could apply some of the increased GPR revenues associated with the recent general fund tax reestimates by this office toward buying down the GPR debt restructuring amounts in 2011-12. This would repay some of the state's GPR debt in that year. Otherwise, any decision to reduce the amount of debt restructuring recommended by the Governor would require further reductions to state GPR aid to local governments and school districts or other GPR-funded state programs in 2011-12, unless general fund taxes were increased.

Proponents of GPR bonding backed programs, especially the state's building program and highway construction program, contend that having a robust state highway program and state building program has a positive impact on construction-related employment and the state's economy as a whole. Others contend that the projects included in the state building program are needed to update and maintain the state's facility infrastructure, and that delaying these necessary projects would only cost the state more in the future due to the level of construction inflation.

Under its 2011-13 building program recommendations, the Building Commission is recommending a lower level of GPR supported bonding available for issue in the 2011-13 biennium compared to recent biennial state building programs. As discussed, even when these amounts are added to the existing GPR supported bonding and the GPR supported bonding included under AB 40, the amount of bonding available in the biennium would be significantly less than average annual amount of GPR supported bonding issued in recent years.

In making decisions regarding the proper level of GPR supported bonding, the Committee should weigh the positive impacts of funding the recommended state building program and the state's GPR-funded programs against the ongoing concerns about the level of state GPR supported debt that currently exists. The Committee may also want to consider the impact that providing the recommended GPR supported bonding levels will have on the ability of the state to make increasing GPR debt payments going forward while continuing to fund GPR program costs within existing revenues in those same years.

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