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# **Overview of State Debt and Lease-Purchase Financing**

**January 29-30, 2013**

**Appropriations Committee Hearings**

**JLBC**

# Statute Requires JLBC to Annually Report on State Debt and Other Obligations

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- ❑ Outstanding principal on State debt, along with principal and interest payments in the prior fiscal year (FY 2012)
- ❑ Summary of payment deferrals (“rollovers”) by budget unit and the cost of these deferrals
- ❑ Information on per-capita State debt and other long-term obligations
- ❑ A 10-year history of State debt and long-term financing based on available data

# Arizona Constitution Limits General Fund Backed Debt to \$350,000

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- ❑ This limit has been interpreted as applying to debt secured by General Fund revenues
- ❑ This interpretation does not apply to debt secured by non-General Fund revenues
  - State has outstanding bonds supported by transportation, lottery and University revenues
- ❑ Lease-purchase financing has also been viewed as not applying to the limit – unlike bonds, there is no dedicated source of repayment

# Lease-Purchase Financing vs. Bonds

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- ❑ Lease-purchase financing has no dedicated source of repayment
  - Lease agreements typically have language that payments are “subject to annual appropriation by the State Legislature” and are not “a general obligation or indebtedness of the State”
  - Non-payment would terminate lease and cause loss of property/project
- ❑ Bonds have a dedicated funding source and are secured by non-General Fund source, such as:
  - Lottery Revenue
  - Highway User Fees
  - University Tuition

# Uses For State Debt and Lease-Purchase Financing

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- State owned capital facilities/uses
- School Facilities Board to fund local new school construction
- During budget shortfalls, financing has been used for operating expenses

# State Has Recently Used Operating Financing For \$1.5 B of Solutions To Budget Shortfalls

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## FY 2010

- ❑ \$1.0 B from the sale and leaseback of 22 state properties
  - Building titles transferred to 3<sup>rd</sup> party – transfers back after 20 years of lease payments
- ❑ \$450 M from the issuance of lottery revenue bonds
  - Debt service paid from General Fund portion of lottery revenues – represents foregone revenues

## FY 2011

- ❑ \$60 M from the refinancing of outstanding SFB lease-purchase agreements

# Arizona's Credit Rating

## - Tied for third lowest among states

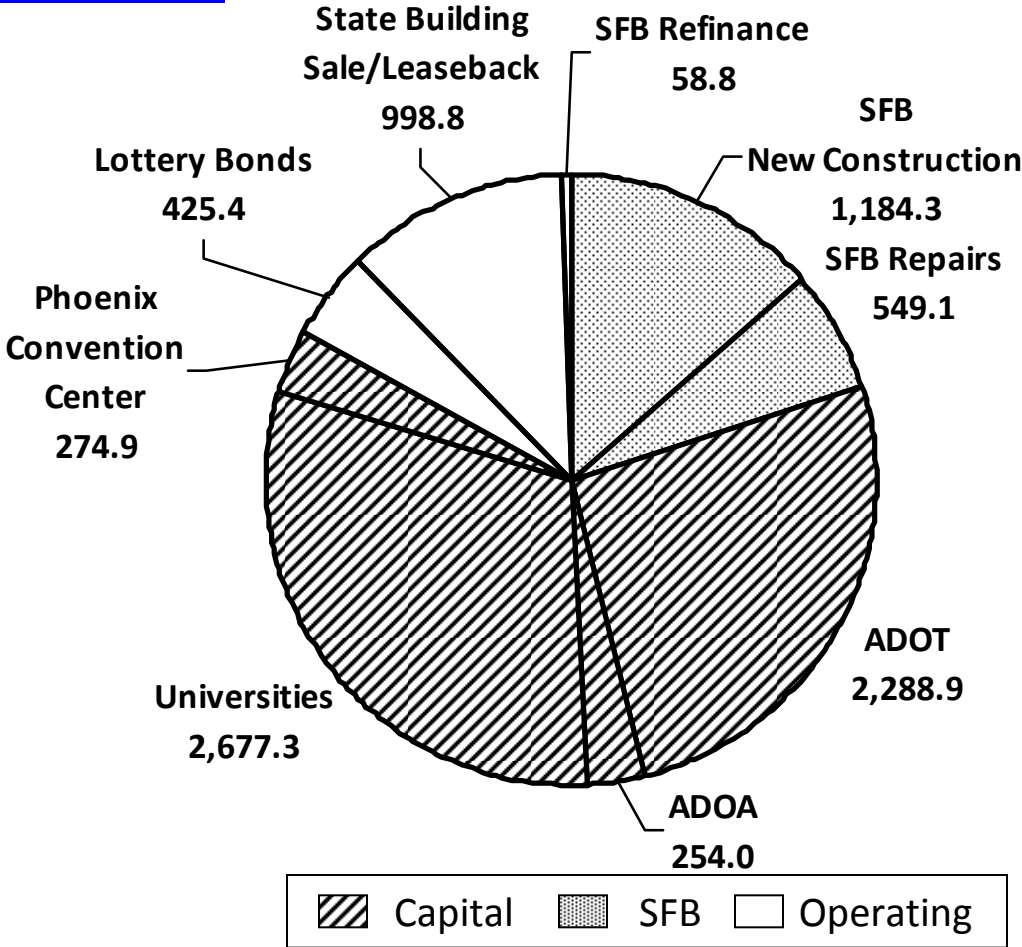
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- ❑ With both major credit rating agencies, Arizona has a similar rating (Standard and Poor's: AA-/Moody's: Aa3)
- ❑ Both agencies' outlook for Arizona rating is stable
- ❑ Rating reports have listed several concerns
  - Limited financial flexibility – Proposition 105 (1998) limits changes to ballot propositions and Proposition 108 (1992) requires 2/3rds vote to increase state revenues
  - Continued economic weakness
  - Concerns about the disposition of short-term budget surpluses
- ❑ However, rating agencies noted moderate debt levels and stabilized financial position as positive trends

# Total Outstanding State Debt/Lease-Purchase Financing is \$8.7 Billion

- Reflects Multiple Payment Sources

Outstanding Balances	
Capital Facilities/Uses	\$ 5.5 B
School Facilities Board	\$ 1.7 B
Operating	\$ 1.5 B

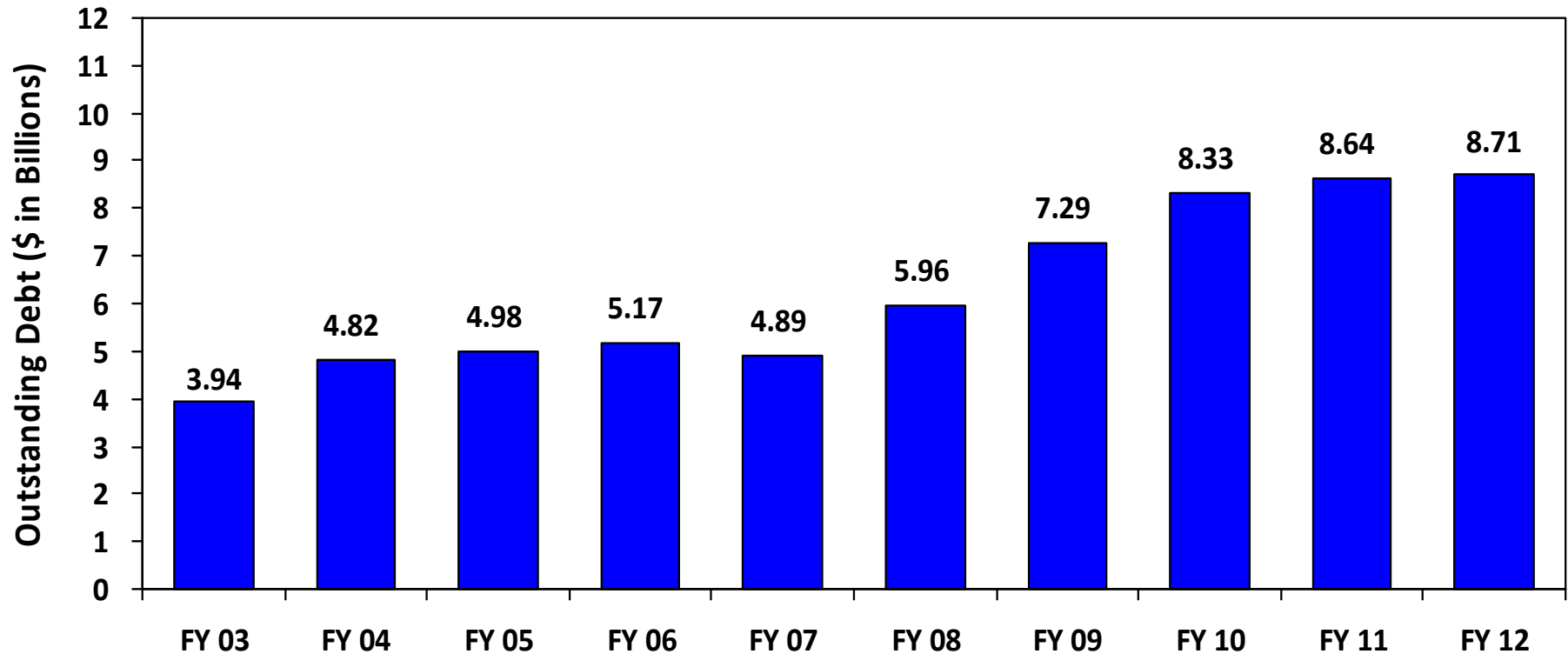


End of FY 2012 - \$ in Millions



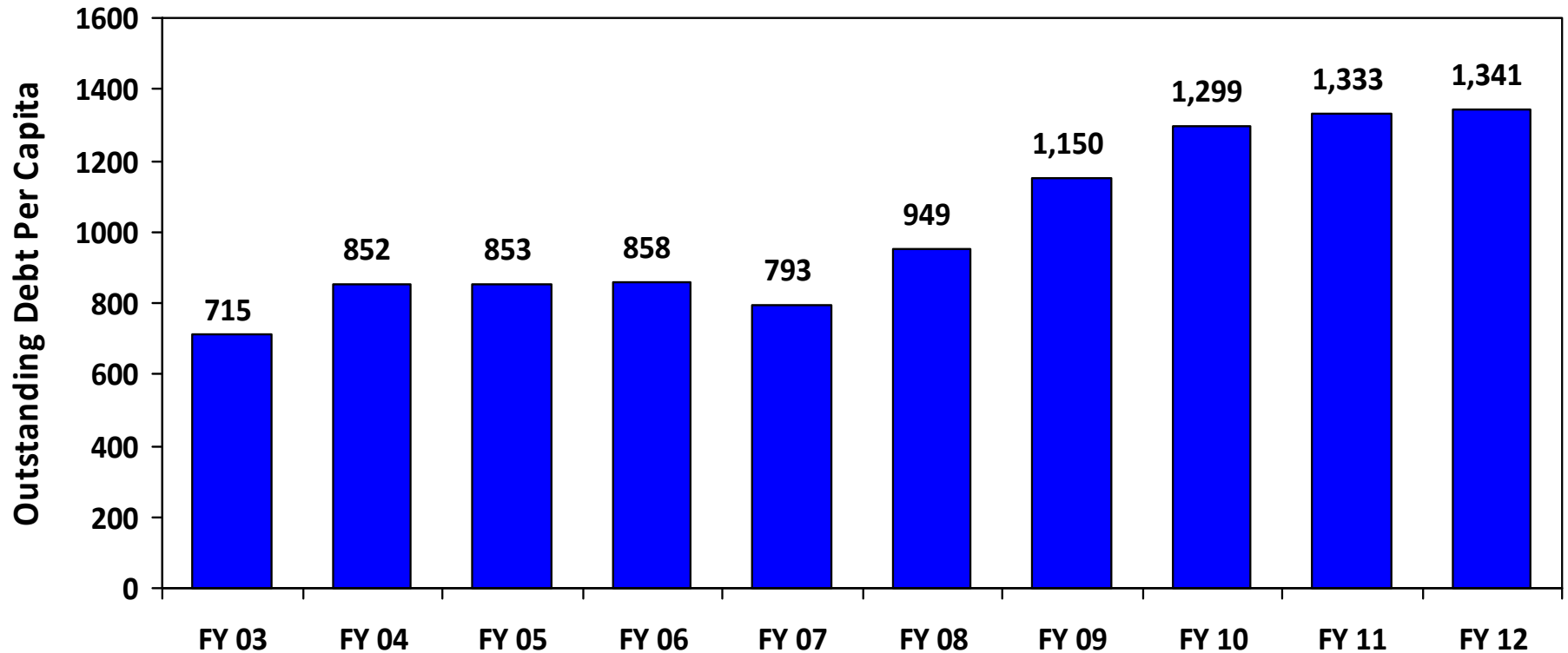
# Arizona Overall Debt Obligations Have Increased Significantly Since FY '07

- Increase Is Mostly Due to ADOT, SFB and Operating Financing



# Arizona Per Capita Debt Obligations Since FY '03

- State's Assumption of Financing K-12 Construction and Recent Operating Financing Played A Major Role In Growth



# State Also Defers \$1.2 B of Payments Annually

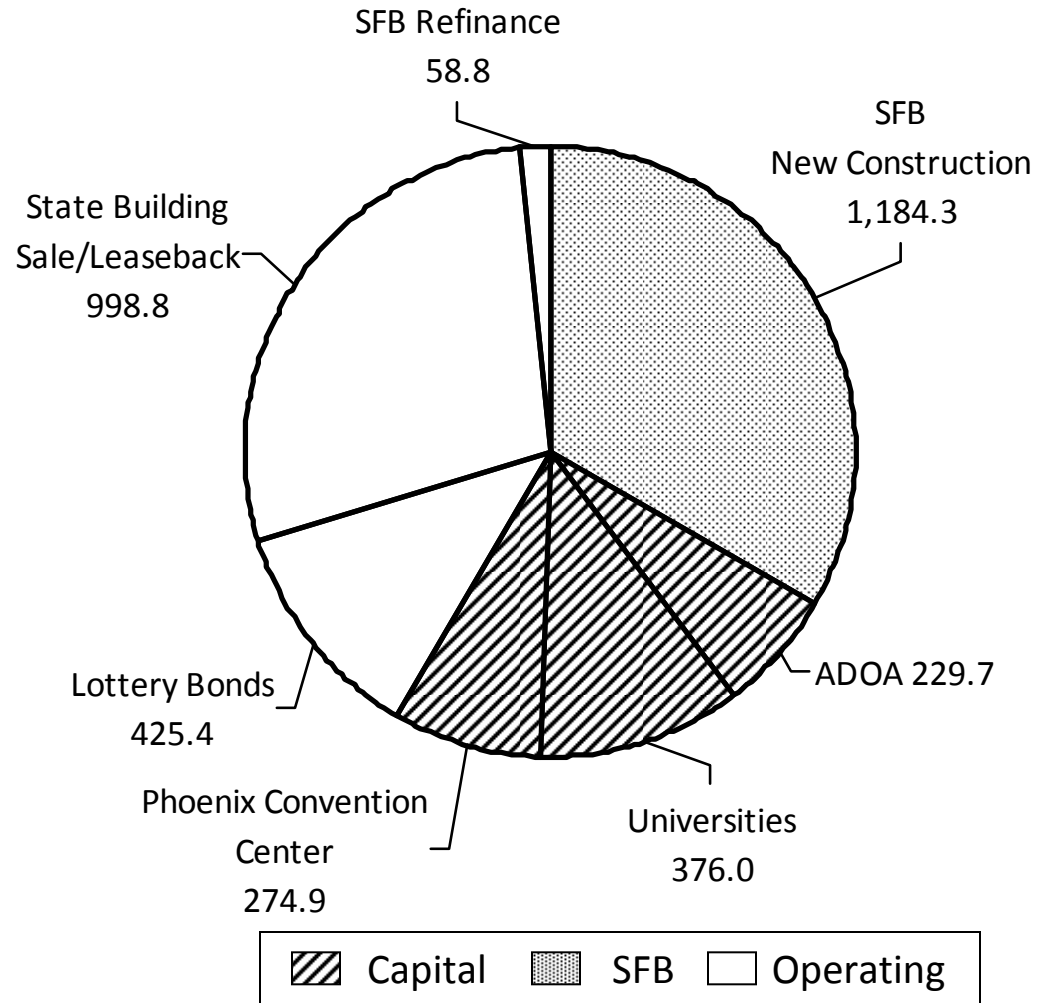
## - Interest Is Not Paid By the State For Rollovers

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- ❑ Used for one-time solutions during recent years with significant budget shortfalls. FY 2013 budget eliminated rollover associated with payments to AHCCCS health plans.
- ❑ K-12 State Aid payments: \$953 M
- ❑ Universities: \$200 M
- ❑ DES: \$35 M

# General Fund Share of Outstanding Balances Is \$3.6 B

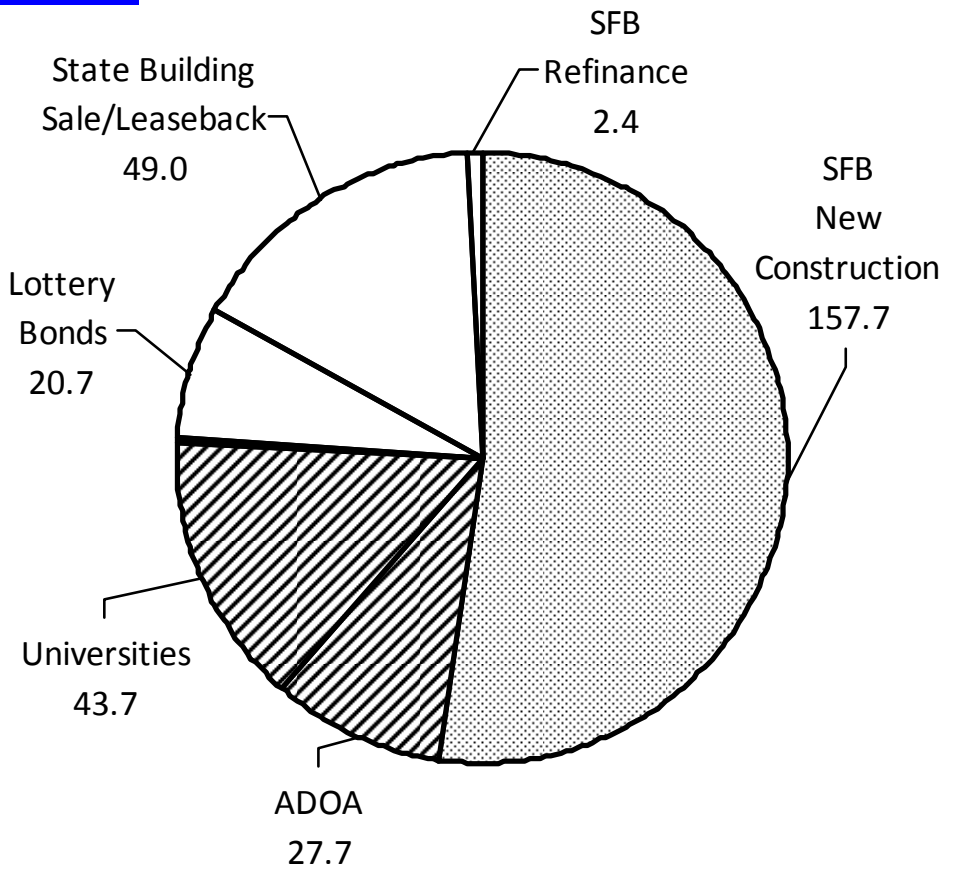
Outstanding Balances	
Capital Facilities/Uses	\$ 0.9 B
School Facilities Board	\$ 1.2 B
Operating	\$ 1.5 B



# General Fund Debt Service Cost \$302 M

## - Represented 7th Largest Budget Unit

Annual Payments	
Capital Facilities/Uses	\$ 72 M
School Facilities Board	\$ 158 M
Operating	\$ 72 M



Capital
  SFB
  Operating

FY 2012 - \$ in Millions

# Annual General Fund Debt Service/Lease-Purchase Financing Costs Will Increase Through FY 2014

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<u>\$ in Millions</u>			
	<u>FY '12</u>	<u>FY '13</u>	<u>FY '14</u>
Capital Facilities/Uses	72	63	77
School Facilities Board	158	167	172
Operating	72	124	124
<b>Total</b>	<b>\$302 M</b>	<b>\$354 M</b>	<b>\$373 M</b>

# Optional Debt Retirement

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- ❑ FY '14 Executive budget includes an on-going \$40 million annually for debt reduction
- ❑ Proposal could include the state's debt/lease-purchase financing or rollovers – no specific debt obligation was identified for retirement.
- ❑ Further analysis would be needed to identify which financing issuance would be most cost-effective to retire based on a variety of financial factors.

# Potential Issues for Debt Retirement

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- ❑ Variety of factors when selecting which issuances should be retired early
  - Call date – Most financing agreements have a time period where the state is prohibited from paying off the outstanding balance, typically 10 years from issuance
  - Principal amount/interest rate – Both of which affect the level of annual debt service
  - Length of term – As financing period become longer, the state generates more savings from avoided payments
- ❑ Transaction costs may affect whether debt retirement occurs in one transaction or over several years



# Mandatory Debt Retirement

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- ❑ In order for the \$1.5 B operating debt issuance to qualify as federally tax-exempt, State must begin to retire balance if cash reserves exceed 5%
- ❑ May not be effective until FY '17
- ❑ Limited examples of these requirements being applied in other jurisdictions – more specific guidance is needed

**Lease-Purchase and Bonding Summary**

	<b>GF Balance After FY 14</b>	<b>Call Date</b>	<b>Interest Rate Range</b>	<b>Retirement FY</b>
<b>2003 Issuances</b>				
School Facilities Board (2003 B)	15,185,000	9/1/2013	4.2% - 5.25%	FY 15
<b>2004 Issuances</b>				
ADC Prison Expansions (2004 B)	13,995,000	Info not available	Info not available	FY 19
School Facilities Board (2004 A)	19,865,000	9/1/2014	5.0%	FY 19
School Facilities Board (2004 B)	43,195,000	9/1/2014	4.25% - 5.25%	FY 17
School Facilities Board (2004 C)	24,860,000	9/1/2014	4.75% - 5.0%	FY 20
ASU Research (2004)	65,455,000	9/1/2014	4.125% - 5.25%	FY 31
NAU Research (2004)	30,445,000	9/1/2014	4.0% - 5.125%	FY 31
U of A Research (2004 A)	275,000	6/1/2014	5.25%	FY 15
<b>2005 Issuances</b>				
School Facilities Board (2005 A1/A2/A3)	320,035,000	9/1/2015	3.625% - 5.0%	FY 20
Phoenix Convention Center (2005 B)	260,124,300	Unable to call	5.50%	FY 44
ASU Research (2005 A)	88,680,000	3/1/2015	3.375% - 5.0%	FY 31
NAU Research (2005)	32,370,000	9/1/2015	3.75% - 5.125%	FY 31
<b>2006 Issuances</b>				
ASU Research (2006)	12,525,000	6/1/2016	4.0% - 5.0%	FY 31
NAU Research (2006)	1,275,000	9/1/2016	4.0%	FY 17
U of A Research (2006)	14,655,000	6/1/2016	4.0% - 5.0%	FY 31
<b>2007 Issuances</b>				
U of A Research (2007 D)	42,630,000	6/1/2017	4.0%	FY 31
<b>2008 Issuances</b>				
ADC 4,000 Prison Beds (2008 A)	162,740,000	Info not available	Info not available	FY 28
ADC Water, and Wastewater (2008 A)	4,815,000	Info not available	Info not available	FY 23
DHS Forensic Hospital (2008 A)	22,790,000	Info not available	Info not available	FY 23
School Facilities Board (2008 A)	454,870,000	9/1/2018	5.0% - 5.75%	FY 24
<b>2010 Issuances</b>				
\$735 M Sale/Leaseback (2010 A)	657,545,000	10/1/2019	4.2% - 5.25%	FY 30
\$300 M Sale/Leaseback (2010 B)	268,070,000	4/1/2020	4.0% - 5.0%	FY 30
Lottery Revenue Bond	391,185,000	1/1/2020	3.5% - 5.0%	FY 29
Federal Bonds	79,909,400	Now, subject to certain conditions	6.0%. State cost after subsidy = 1.14%	FY 28
2011 Refinance	58,785,000	Unable to call	3.0% - 5.0%	FY 20
<b>2012 Issuances</b>				
U of A Research (2012 C)	98,920,000	6/1/2022	5.0%	FY 31
<b>Total</b>	<b><u>3,185,198,700</u></b>			