# Overview of State Debt

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# What Are Bonds?

- Bonds are the most common, but not the only, form of debt. Capital leases are also debt.
- A bond is a debt investment, with which the investor loans money to an entity (such as a company or government) that borrows the funds for a defined period of time at a specified interest rate.
- A lease that meets at least one of the following criteria is a capital lease:
  - Ownership is transferred at the end of the lease.
  - Lease allows for a low price purchase at fixed terms.
  - Term is 75% of useful life.
  - Present value of lease payments is 90% fair market value.

# Why Sell Them?

- Advantages associated with selling debt to support capital construction include:
  - Use an asset sooner.
  - Align asset use with expenditure.
  - Bond financing allows future users to share paying for the asset.
- Disadvantages associated with selling debt to support capital construction include:
  - Project costs increase.
  - Bonds are a long-term liability.

# Categories of State Debt

General Obligation Bonds

Federal Tax Credit and Direct Payment Bonds

Capital Leases

Revenue and Bond Anticipation Notes

Transportation Debt

Grant Anticipation Revenue Vehicles

Stadium Authority Bonds

Bay Restoration Bonds

# General Obligation Bonds

- The General Assembly authorizes the State to incur debt for specific capital projects, generally consolidated into one bill known as the Maryland Consolidated Capital Bond Loan (MCCBL).
- The Board of Public Works authorizes the issuance of general obligation (GO) bonds and expenditure of bond proceeds, structured at issuance to mature in 15 years (interest only payments in first 2 years, with equal annual principal and interest payments for remaining 13 years).
- When issuing a GO bond, the full faith and credit of the issuer is pledged.

# Capital Leases

- Capital leases are defined by GAAP*.
- Types of leases include:
  - Property
  - Equipment
  - Energy
- Leases are State debt if the revenues supporting the lease is a State revenue.

* Generally Accepted Accounting Principles

# Federal Tax Credit and Direct Payment Bonds

- The State has issued Qualified Zone Academy Bonds (QZABs), Qualified School Construction Bonds (QSCBs), Qualified Energy Conservation Bonds (QECBs), and Build America Bonds (BABs).

- The State issues the bonds and the buyers can receive federal tax credits or the State will receive a direct payment to offset interest costs.

- QZABs, QSCBs, and QECBs have been issued to support educational capital projects. BABs can support the same projects that tax exempt bonds support.

# Transportation Debt

- The Maryland Department of Transportation (MDOT) issues tax-supported debt for a variety of transportation projects, including highways, mass transit, and airports.
- Debt service for consolidated transportation bonds is payable from the Transportation Trust Fund.
- MDOT debt must meet these criteria:
  - statutorily established debt limit that is currently $2.6 billion; and
  - annual net revenues and pledged taxes must equal at least twice the maximum future debt service, as noted in the Official Statement.

# Other Transportation Debt

- Grant Anticipation Revenue Vehicles (GARVEE) (bonds backed by expected future federal revenues)

- Non-traditional debt (which are often capital leases)

- Debt backed by customer facility charges, passenger charges, or other revenues

- Revenue bonds issued by the Maryland Transportation Authority or the Maryland Economic Development Corporation on behalf of MDOT

# Maryland Stadium Authority

- The Maryland Stadium Authority (MSA) was established to build, maintain, and operate baseball and football stadiums at Camden Yards in Baltimore City. MSA was authorized to issue up to $235 million in revenue bonds to pay for the construction of the stadiums.

- Through separate legislation, MSA was authorized to issue revenue bonds for the construction of the Baltimore City and Ocean City convention centers, a conference center in Montgomery County, the Hippodrome Theatre in Baltimore City, and the renovation of Camden Station.

- Debt service payments are supported by the general fund and lottery proceeds.

# MD Water Quality Financing Administration Bay Restoration Fund Bonds

- Established as a unit of the Maryland Department of the Environment (MDE), the Maryland Water Quality Financing Administration (MWQFA) is authorized to issue Bay Restoration Fund bonds to provide financing to upgrade wastewater treatment facilities.

- Bay bonds are not backed by the full faith and credit of the State but are considered State debt since they are backed by a fee imposed by the State through its general taxing power.

# MD Water Quality Financing Administration Bay Restoration Fund Bonds (cont.)

- There is currently no limit on the amount of Bay bonds that MWQFA may issue.

- Before issuing bonds, MWQFA must first seek the approval of the MDE Secretary and the Board of Public Works.

# Capital Debt Affordability Committee Created to Evaluate Bonds' Affordability

- Selling bonds creates a long-term liability that needs to be acknowledged on the State's balance sheet.

- To manage this liability, the State created the Capital Debt Affordability Committee (CDAC) in 1978.

- CDAC is chaired by the State Treasurer. Other committee members are the Comptroller, Secretary of Budget and Management, Secretary of Transportation, and a public member appointed by the Governor. The chairs of the capital budget subcommittees in the House and Senate are nonvoting members of the committee.

# CDAC Created to Evaluate Bonds' Affordability (cont.)

- Sections 8-101 to 8-114 define the duties of CDAC, which include reviewing State debt and recommending prudent debt authorizations.
- State debt includes:
  - GO bonds;
  - Federal tax credit and direct payment Bonds;
  - Capital leases supported by State revenues;
  - Bond and revenue anticipation notes;
  - Transportation bonds;
  - Grant Anticipation Revenue Vehicles (GARVEE);
  - Stadium Authority bonds funded with State revenues; and
  - Bay restoration bonds.

# CDAC Created to Evaluate Bonds' Affordability (cont.)

- Maryland agencies also sell debt that is not considered State debt. This includes bonds sold by authorities (such as the Maryland Transportation Authority) and higher education facilities. Debt without State revenue support or pledges (such as debt supported by airline passenger facility charges) is also not considered State debt. CDAC does not include non-State debt in its limit.

- CDAC must submit its recommendations by October 1. Along with its recommendations, it also submits a report. CDAC's recommendations are advisory and non-binding. The Governor is required to consider CDAC's recommendations when making the statutorily required November preliminary allocation.

# CDAC Created to Evaluate Bonds' Affordability (cont.)

- CDAC has developed the following criteria to measure affordability:
  - Total outstanding State-tax-supported debt should not exceed 4% of State personal income.
  - Debt service on State-tax-supported debt should not exceed 8% of revenues.

# After CDAC

- The Spending Affordability Committee reviews the CDAC recommendation and recommends a prudent level of GO bond debt.

- The Administration submits its capital budget (MCCBL) by the twentieth day of the legislative session.

- The legislature passes the capital budget bill. The Maryland Constitution requires that the operating budget be enacted before the legislature can pass the capital budget.