The Office Of State Treasurer
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Statement

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Budget Advisory on Bonding and Debt Service

The General Assembly and Governor Malloy are in the midst of evaluating options for addressing a projected deficit for Fiscal Year 2017. Questions have been raised as to whether limitations on bond issuance, capital spending, or both could result in meaningful debt service savings, enough to help close the gap.

The purpose of this Budget Advisory is to respond to those questions and to highlight important principles and considerations that may inform deliberations concerning the ultimate budget solution.

Capping bond issuance in Fiscal Year 2017

Limiting the amount of bonds issued during FY17 will not result in debt service savings until future fiscal years. It will have no impact on the FY17 debt service budget because bonds issued in FY17 do not have debt service due until the next fiscal year and subsequent fiscal years. There is, however, one FY17 semi-annual interest payment due, which is projected to be covered by bond premium, not the debt service line item in the General Fund budget.

In fact, reducing bond issuance would actually increase the need to fund debt service from the General Fund in FY17 because less bond premium from bond sales would be available to help pay for debt service.

Limiting the amount of bond projects authorized by the Bond Commission

Expenditures on bond funded projects are for ongoing projects that have previously been authorized by the Bond Commission. Even limiting the amount of bond projects authorized by the Bond Commission during FY17 would likely have a limited impact in FY17 given the normal delay between authorization and actual commencement of capital projects.

Capping the amount of bonds issued in FY17 will not, by itself, reduce expenditures on bond funded projects for FY17.

Potential cash crunch

Limiting the amount of bonds issued in FY17 without reducing expenditures on bond funded projects, will result in a State cash deficit and the inability to fund projects or other expenses without temporary borrowing.

If bond issuance is limited and expenditures on bond funded projects continue at their current higher pace of $2 billion annually, the State's cash resources would have to cover bond project expenditures, thereby draining cash resources and depleting the ability to fund State obligations without implementation of temporary borrowing. Such a step would be of significant concern to rating agencies and bond investors.

To illustrate the severity of this action on the State's cash flow, there is approximately $700 million in bond proceeds deposited at the Treasury. Assuming no more bonds are issued and applying this amount to the annual bond proceeds spending of $2 billion results in the exhaustion of the bond proceeds account in August of 2016.

Reducing Costs

In order to reduce bonding without negative impact, expenditures on bond funded projects must be reduced and the spigot needs to be turned off at the source.

Currently, $2.8 billion worth of projects have been authorized by the Bond Commission that have yet to be funded with General Obligation bonds. The only effective way to reduce expenditures on these projects would be for the State agency involved to halt those projects that have not begun, or can be stopped under contractual terms.

In addition, the State would need to stop authorizing new spending on bond projects, thereby reducing the amount of bonding needed to fund the projects.

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