TO:	The Honorable Tate Reeves, Chairman, JLBC
	The Honorable Philip Gunn, Vice Chairman, JLBC
	All members of the JLBC
	Tony Greer, Director, LBO
FROM:	Treasurer Lynn Fitch
DATE:	Thursday, September 21, 2017
RE:	FY2019 Budget Hearings

I regret that when the invitation to attend this hearing was received by my office last week, I already had a previous engagement on my calendar that could not be rescheduled. However, I appreciate the opportunity to share with you the information you have requested about the State's Debt Service Budget Request for Fiscal Year 2019. As always, my staff and I are available to answer any question or discuss any of these issues throughout the year.

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FY19 Request as Submitted:

My office submitted the following budget request for FY19:

General Fund (22951)	$437,143,611.00
Special Funds (63951)	$ 35,845,502.00
Revenue (63980)	$ 16,122,350.00
	$489,111,463.00

In historical context:

	FY17 Actual	FY18 Estimate	FY19 req vs FY17 actual
General Fund	$392,189,838.00	$385,241,392.00	increase $44,953,773.00
Special Funds	$103,050,847.00	$ 85,879,828.00	decrease $67,205,345.00
Revenue bonds	$ 13,097,350.00	$ 14,775,375.00	increase $ 3,025,000.00
TOTAL:	**$508,338,035.00**	**$485,896,595.00**	**decrease $19,226,572.00**

As you know, debt service requests are always estimates based on historical data and analysis. In particular, our special funds level is dependent on the fluctuations of financial markets, making it impossible to know precisely what may be available for debt service a year and a half ahead of the actual date.

Furthermore, the Bond Commission is currently planning the Fall 2017 bond sale, which will likely alter the needs for debt service appropriations in FY19. Once that sale is final, we will provide fresh numbers to the JLBC.

Unlike other agency budgets, the annual debt service request is dependent on payment schedules pursuant to the general obligation debt authorized by the Legislature and issued by the Bond Commission. It does not represent salaries or overhead that can be cut; it does not represent programs which can be streamlined or delayed. While the Bond Commission can take steps to refinance debt to achieve some savings, as we did in June 2017 to achieve $34 million in taxpayer savings, there are no other options at the Commission's disposal to alter the overall trajectory of these numbers.

Use of Special Funds:

Increased Costs to Taxpayers: As I have indicated in previous correspondence with this committee and with the Legislature, increasing reliance on special funds to pay annual debt service has depleted our special funds dramatically. Without a balance in special funds, the State has no capacity for short-term borrowing. That means when short-term borrowing is necessary, we have to go to outside sources, which incurs greater costs of taxpayers.

Continental Tire is a good example. Last year, after extensive conversation with MDA, the Bond Commission engaged in $80 million of short-term borrowing for that project. This was based on the anticipated needs of the project over the course of the year, the expected schedule for those expenses, and a desire to keep the cost of money for the State as low as possible. In past years, we would have had sufficient special funds to meet that short-term borrowing request. We no longer have that capacity so the State had to go to a bank, with its fees and interest, to accommodate the short-term borrowing needs to get the Continental Tire project started.

What is Available: The amount of special funds requested for FY19 is based on our anticipated balances as of June 30, 2019, which may increase or decrease as the fiscal year progresses. My office will keep you updated throughout the year on the status of these funds, as we do every year. This will ensure that when the Legislature is ready to pass the FY19 debt service budget, it is using the most up-to-date numbers.

The full balance of the special funds account is not an accurate depiction of the funds available to pay debt service in a given year. Because of the language of bond documents that accompany issuances and other legal requirements, there may be additional money in the special funds account, but on paper only, as it can only be used to repay specific debt. For example, we anticipate a nearly $57 million balance on June 30, 2019 related to Build America Bonds (BABs), but that sum cannot be used for other, unrelated debt.

Deficit Appropriations:

We share your interest in establishing a realistic budget that reduces and even eliminates the need for deficit appropriations. The amounts we have provided in our FY19 budget request are based on what we believe can be achieved and if authorized and appropriated as such should result in no deficit appropriations for FY19 debt service.

As you know, in the past two years, we have had narrow misses with regard to deficit appropriations. The amount authorized from special funds in FY17 left us with a substantial deficit. We were able to mitigate that by (1) specifically structuring the December 2016 bond sale to achieve some savings in that fiscal year, and (2) receiving an unanticipated, early repayment of an MDA program loan.

Similarly, the Bond Commission was able to eliminate the need for a deficit appropriation for FY18 by specifically structuring a refunding in June 2017 to achieve $33 million of $34 million in savings in this fiscal year and to eliminate the need for a deficit appropriation.

Structuring bond sales, whether they are new money, refundings, or refinancings, in order to mitigate shortfalls in appropriations limits the ability of the Bond Commission to achieve the best possible sale for the State. It forces us to prioritize the timing of savings over the savings themselves.

Similarly, early loan repayments are a great benefit to the State in that they can help to plug shortfalls, but they cannot be anticipated and therefore they cannot be relied upon.

<u>Future Debt:</u>

I am attaching to this report the list of debt that the Legislature has authorized, but the Bond Commission has not yet issued as of June 30, 2017. This list totals over $1 billion in authorized borrowing. DFA has been working to reconcile the list and the attached is fully reconciled to the current date, with the exception of the MDA MMEIA program, which is presently being reconciled.

In addition, while the Legislature did not pass a “bond bill,” per se, in the 2017 Regular Session or 2017 Extraordinary Session, it did authorize new debt this year for MDA programs in SB 3033. HB 1729, the 2016 Bond Bill, also included over $50 million in projects which were not authorized until this fiscal year. As a result of these new authorizations and the extensive authorized, but unissued list, the Bond Commission is currently preparing for a December bond issuance of approximately $90 million.

<u>Debt Clean-Up:</u> In the past, the Legislature has worked with the Bond Commission to clean up outstanding authorizations; that is, to verify which outstanding authorizations are no longer necessary to eliminate them from the list even before their legislated expiration date. As you review the list of authorized, but unissued debt I have attached here, you may agree that it is time to do so again. We stand ready to do our part to fulfill this goal. As you know, an outstanding list of hundreds of millions of dollars in authorized new debt concerns credit rating agencies; whereas regular debt clean-up is a smart management practice that the agencies like to see.

In addition, I have attached a list of previously authorized and issued debt that has still not been used by the requesting agencies. The list totals over $590 million. The funds represent a variety of projects for a variety of agencies, including IHL, DFA- Bureau of Buildings, and MDOT. When an agency requests that the Bond Commission issue bonds in accordance with a legislative authorization, there should be an expectation that the project is shovel-ready because once issued, the State begins paying interest on the debt. However, many agencies have voiced concerns about having the funds available when they are ready to go and they ask for issuance early to be on the safe side. I do understand their interest in finding the right balance, but there needs to be more vigilance in ensuring we are not being overly cautious to the taxpayers' detriment.

Additionally, there is some discussion now about how the actual language used for authorizing debt might encourage earlier issuance than is necessary. As currently crafted, projects will receive not only the funds authorized but also any interest those funds accumulate before they are drawn down. Thus there is a built-in incentive to encourage early issuance. Taxpayers are paying interest on the debt, but are not benefiting from any interest accrued on the funds before they are used.

There are two potential solutions to these issues. One lies in rebuilding our special funds reserve so that we can provide interim, short-term borrowing for agencies trying to find the right timing for their project's financing. The other lies in rewording authorizations so that interest accrued on funds sitting unused goes to our sinking funds for use in paying debt service. Again, my office stands ready to address these issues with the Legislature.

Our Credit Ratings: As JLBC noted in preparation for the 2017 Regular Session, debt service is the third largest item in our State budget. In its annual debt analysis, Moody's increased Mississippi's Net Tax Supported Debt per capita substantially. **Whereas last year, every Mississippi man, woman, and child carried a debt burden of $1,707, this year, each carries $1,847.**

Our credit ratings now stand at:

Moody's	Aa2 negative
Standard & Poors	AA negative
Fitch Ratings	AA stable

Our ratings are like our State's credit score. They determine the cost of borrowing for our State. Better scores mean lower costs for Mississippi taxpayers. The rating agencies share information in these reports that can help to guide our fiscal policies, and I encourage you all to read these latest reports if you have not done so already.

The agencies include information about trends in our State policies and demographics that are a cause for concern, as well as those in which they find encouraging signs. The reports are a roadmap to improving our credit ratings and saving Mississippi money. All three credit rating agencies reviewed the State finances this year and all three noted our higher than average debt as a reason for concern.

Debt Management Tools: Last fall, the Bond Commission adopted new debt management rules drawn from best practices used in other states. These rules can be a helpful guideline for fiscally conservative borrowing practices for the Legislature, for the Bond Commission, and for anyone seeking an authorization to borrow on the taxpayers' credit card. They can be found at Title 12, Part 7, Chapter 1, Rule 1.2A of the Mississippi Administrative Code.

Similarly, the annual debt affordability study that I release to the Legislature and the public each year is meant to be a tool for the Legislature to use when you are making decisions about future debt. Tools like these are considered by credit rating agencies to be positive evidence of a proactive approach to debt management and receive favorable consideration.

<u>New Language for This Year's Debt Service Appropriations Bill:</u>

During Senate debate on the FY18 debt service appropriations bill, there was some discussion about what "bank fees" includes and some concern that the State was budgeting for $500,000 in bank fees. These concerns arose from a misunderstanding of what bank fees really means in this context. It is not merely what individuals or even companies typically incur for day-to-day banking, like ATM withdrawal fees or checking fees. It includes sums we pay for determining arbitrage as required by federal law, as well as for financial services incurred as a result of bond issuances.

In FY18, as well as FY19, we reduced this amount from $750,000 to $500,000 to reflect the fact that we have rarely approached that higher level in a given year. Funds not used revert to the General Fund at the end of the Fiscal Year.

To avoid this confusion in future debates, I recommend renaming "bank fees" with something more descriptive of their true purpose, such as "debt management fees."