The Missouri Budget Project

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New State Bonding Proposal in Need of Thorough Review

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House Joint Resolution (HJR) 77 was filed on January 14, 2010 in the Missouri Legislature. This proposal would allow Missouri (with voter approval) to issue up to $800 million in bonds for capital improvement projects, with a minimum of $550 million of the bonds to be allocated to both two and four year public higher education institutions in Missouri. The bonds would be paid back over a 25 year period.

Should the bonds be issued under the *Build America Bonds* program, the state would be eligible to receive a federal subsidy of 35 percent of the interest it pays, although the earnings would be taxable for those investing in the bonds. The state could also choose to issue these as traditional general obligation bonds, which generally carry a lower interest rate than taxable bonds but are tax exempt for those investing in these bonds.

There is little doubt that the last ten years of mostly lean state budgets have left Missouri with a substantial backlog of much needed capital improvement projects. This need has been especially acute for the state's higher education institutions, all of which have major investments in physical plants which require maintenance and periodic replacement.

In addition, the interest rate subsidy that is available via the *Build America Bonds,* coupled with relatively attractive market rates of interest, could make this a favorable time for the state to issue new debt to fulfill some of these needs. However, it is important to evaluate this proposal in the overall context of the state budget outlook in order to determine if the state will have the resources needed to meet new bonding debt.

Missouri's Current 2010 Debt

While the Missouri Constitution prohibits borrowing money for use in the operating budget, the state is allowed to and does issue bonds for a variety of capital improvement, transportation and infrastructure projects. The bonds issued by the state fall into four categories, which include those in Table 1 below.

Table 1: Summary of Missouri Bond Series As of July 1, 2009[1]	
Bond Type	**Outstanding Principle Amount**
General Obligation Bonds	$600,075,000
Revenue Bonds	$623,330,000
Other Appropriation Debt Payments	$317,584,000
Transportation Debt Payments	$2,355,925,000
TOTAL	**$3,896,914,080**

[1] Missouri Office of Administration

As of July of 2009, the state had existing debt obligations of just under $3.9 billion in the four major categories described below:

General Obligation Bonds consist of bonds issued for water pollution control, storm-water control, as well as the Third and Fourth State Building funds. These debt obligations extend to the year 2033, and are repaid with general revenue, appropriated through House Bill 1 annually.

Revenue Bonds consist of the obligations of the Board of Public Buildings. These payments are made primarily with general revenue and are part of the Office of Administration Budget in House Bill 5.

Other Appropriation Debt Payments consist of a variety of state obligations including the debt service on the Edward Jones Dome in St. Louis and the Mizzou Arena in Columbia. These payments are made primarily with general revenue and are part of the Office of Administration Budget in House Bill 5.

Transportation Debt payments are for debt service on road and bridge projects. A substantial portion of this debt is associated with the bonding program authorized by Amendment 3, which was approved by voters in November of 2004. This debt is being serviced by the motor vehicle sales tax, which now accrues entirely to MODOT.

The principal and interest payment schedule for all of Missouri's statewide current debt obligations will require payments totaling more than $4 billion by 2020 (See Table 2 below). For the next several years, this debt requires payments made from Missouri general revenue of nearly $200 million for non-transportation related debt. By the year 2017, general revenue payments for current non-transportation debt will dip somewhat to $135 million.

HJR 77 would allow Missouri to increase the debt amount by an additional $800 million. Assuming that the state would receive bonds with a 4 percent interest rate under a repayment schedule of 25 years, HJR 77 would increase Missouri's general revenue debt by an additional $51 million per year.

Table 2: Current State Debt Repayment Requirements by state fiscal year in millions[2]						
Fiscal Year	General Obligation Bonds	Revenue Bonds	Other Appropriation Bonds	Total Non-Transportation Bonding	Transportation Bonds	Total State Bonding Debt
2007	$89.4	$54.8	$34.3	$178.5	$125.0	$303.5
2008	$97.6	$62.2	$34.3	$194.1	$152.7	$346.8
2009	$95.4	$61.7	$34.3	$191.4	$198.9	$390.3
2010	$98.1	$61.3	$40.3	$199.7	$200.9	$400.6
2011	$92.0	$51.7	$40.3	$184.0	$208.4	$392.4
2012	$78.3	$51.4	$40.3	$170.0	$224.9	$394.9
2013	$69.4	$50.9	$39.7	$160.0	$228.8	$388.8
2014	$61.9	$48.5	$39.6	$150.0	$229.3	$379.3
2015	$62.2	$48.3	$39.6	$150.1	$229.9	$380.0
2016	$59.2	$48.0	$32.8	$140.0	$222.6	$362.6
2017	$57.8	$47.8	$29.9	$135.5	$222.6	$358.1
2018	$32.8	$47.7	$29.9	$110.4	$222.6	$333.0
2019	$30.1	$47.6	$29.9	$107.6	$222.4	$330.0
2020	$27.9	$47.5	$21.0	$96.4	$222.6	$319.0
TOTAL	**$669.7**	**$550.7**	**$383.3**	**$1,603.7**	**$2,435.0**	**$4,038.7**

The State Budget Outlook

Issuing debt to pay for buildings, transportation projects and other types of capital improvements often represents sound fiscal management. Unfortunately, it is not clear that Missouri will have the financial wherewithal available to pay for the additional debt for the next 25 years.
It is widely acknowledged by Missouri state budget experts that the current general revenue budget outlook is bleak. A careful look at the state budget outlook for FY 2011 and beyond is quite sobering.

Based upon the budget proposed by Governor Nixon on January 20th, combined with the most recent data on revenue collections, the Missouri Budget Project (MBP) has projected a $1.2 billion state general revenue shortfall by FY 2012. Several factors indicate that this gap could be even larger than currently anticipated, including:

- The FY 2011 budget assumes an additional $300 million in federal assistance, which has not yet been approved by Congress; and
- January net general revenue collections declined by 22.4 percent, making it possible that Missouri may not reach the revenue level that the current budget is based upon. In response, Governor Nixon has announced additional mid-year spending restrictions of $74 million.

Without significant improvement in the national and state economy, leading to renewed revenue growth, or a substantial amount of additional federal assistance, Missouri will face a severe funding shortfall within the next year. The state will struggle to fund the services it currently provides including K-12 education, higher education, transportation, health and mental health,

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[2] IBID

and child protection services. New debt at this time would further reduce the ability of Missouri to invest in these core services.

MOHELA: Missouri Higher Education Loan Authority and Capital Improvements

In 2006, Governor Matt Blunt developed and advocated for a plan that sold a substantial portion of the Missouri Higher Education Loan Authority's (MOHELA) financial assets in order to finance a package of capital improvement projects at Missouri public higher education institutions. While the initial plan was met with considerable opposition, a compromise was reached that called for the sale of about $350 million of MOHELA assets. Unfortunately, the current recession coupled with problems in financial markets, have caused a substantial decline in the value of MOHELA's financial assets. This, in turn, has forced MOHELA to suspend a portion of its payments, and suspend some of the scheduled capital improvement projects. The current status of the MOHELA-funded projects is detailed in Table 3 below.

Table 3: Status of MOHELA Projects[3]	
Project Status	Project Amount
Completed Projects	$86.1 million
Continuing Projects	$130.7 million
Partially Continuing Projects	$56,3 million
Suspended Projects	$77.2 million
TOTAL	**$350.3 million**

Given the uncertainty facing financial markets, the future of both the partially continuing and the suspended projects is ambiguous. However, the MOHELA initiative, upon completion of the "proceeding" projects, will have provided $216.8 million in the past two years for higher education capital improvement needs and may provide additional funding in the future.

University of Missouri System Issuing Capital Improvement Bonds

In addition to the funding for capital improvements provided by the MOHELA initiative, in July of 2009, the University of Missouri (UM) system announced that it had issued $332 million in bonds to finance facility projects on its campuses in Columbia, Kansas City, Rolla and St. Louis.[4] The projects include both new construction as well as existing facility improvements. Of these bonds, $256.3 million are *Build America Bonds* and $75.8 million are traditional tax-exempt bonds.

The debt payments on the new bonds issued is $20 million per year and is paid from the UM system's campus operations budget. Combined, the MOHELA initiative and the recent UM system bond have funded approximately $549 million in recent capital improvements at Missouri higher education institutions.

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[3] IBID

[4] University of Missouri, July 16, 2009 News Release

Summary

HJR 77 has both advantages and disadvantages. The Missouri budget struggles over the last decade combined with suspension of portions of the MOHELA initiative have resulted in minimum investment in capital improvements for higher education and other priorities.
In addition, interest rates are likely to remain low by historical standards over the next few years, therefore lowering the costs to the state if it takes on additional debt. Finally, issuing debt for long term capital improvements and other infrastructure may often be sound fiscal management.

However, HJR 77 must be evaluated in the overall context of the Missouri state budget situation. Unfortunately, the budget outlook is precarious. In fact, the consensus revenue estimate for FY 2010 general revenue is nearly 9 percent lower than general revenue in FY 2000 when adjusted for inflation.[5] In addition, the state operating budgets for fiscal years 2009 through 2011 (as proposed by the Governor) include approximately $2.5 billion in federal Stimulus funds from the *American Recovery and Reinvestment Act (ARRA)*.[6] When the *ARRA* funding is no longer available in FY 2012 and beyond, the state will face a budget shortfall close to $1.2 billion, even when assuming that general revenue returns to a 5 percent growth rate. While an economic upturn will ameliorate this to some extent, the erosion of the state tax base over the last decade will make it difficult for the state to provide basic services, much less shoulder additional debt service.

State policy makers must begin to come to grips with the reality of the state budget situation and look for a balanced approach to returning to an adequate and sustainable budget. Relying strictly on spending reductions and additional debt may only briefly postpone the inevitable need for long term solutions. The state most certainly cannot solve its structural budget problems by incurring additional debt. It is vital that a HJR 77 type proposal be evaluated in this context.

The Mission of the Missouri Budget Project is: To advance public policies that improve economic opportunities for all Missourians – particularly low and middle-income families – by providing reliable and objective research, public education and advocacy. More information is available at www.mobudget.org.

[5] Missouri Budget Project calculations utilizing data on general revenue collections from the Missouri Executive Budgets series from FY 2000 - FY 2011 and the Bureau of Labor Statistics inflation data.
[6] Executive Budget FY 2011