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California's Debt Burden

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**Joint Legislative Budget Committee
and the
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Bonded Indebtedness and Methods of Financing**

Senators Mike Thompson and Lucy Killea, Chairs

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State Borrowing
Glossary of Key Terms

Term	Description
General Definitions	
Debt	Monies that the General Fund has borrowed and owes to its creditors. Includes both long-term and short-term borrowings.
Deficit	End-of-year excess of budget expenditures over available resources (including revenues and carry-in balances). Represents the cumulative sum of all prior and current operating deficits. Similar in concept to the "national debt" at the federal level.
Operating Deficit	Excess of spending over revenues in any given fiscal year. Similar in concept to the "budget deficit" at the federal level.
Short-Term Debt	
Borrowable Resources	Amounts that the General Fund can use to meet its cash-flow needs.
Unused Borrowable Resources	Borrowable resources available to the General Fund which have not yet been used. Includes both unused internal and externally borrowed resources.
Internal Borrowing	General Fund short-term borrowing from other state special funds, such as funds into which transportation-related revenues are deposited.
External Borrowing	General Fund short-term borrowing from investors, usually through the issuance of notes or warrants.
Revenue Anticipation Notes (RANs)	Issued to provide needed cash in anticipation of receiving revenues later within the same fiscal year.
Revenue Anticipation Warrants (RAWs)	Issued to provide needed cash in anticipation of receiving revenue in the following fiscal year.
Long-Term Debt	
General Obligation Bonds	Long-term bonds generally used to finance major capital outlay projects. Require voter approval, and the General Fund is obligated to pay debt service.
Lease-Payment Bonds	Long-term bonds used to finance major capital outlay projects in lieu of general obligation bonds. Do not require voter approval. Lease payments are annually appropriated to cover debt-service costs.
Revenue Bonds	Generally long-term bonds used to finance major capital outlay projects. Debt service is paid from project-related revenue streams.

Types of State Borrowing

	Maturity	Purpose	Source of Repayment
Short-Term			
RANs	Less than one year	Manage *intra*-year cash-flow needs	General Fund
RAWs	Up to two years	Manage *inter*-year cash-flow needs, including short-term deficit financing	General Fund
Internal Borrowing	Varies	Manage *both intra*-year and *inter*-year cash-flow needs	General Fund
Long-Term			
General Obligation Bonds			
General Fund	Varies, up to 30 years	Finance capital facilities in a wide variety of areas	General Fund
Self-liquidating	Varies, up to 35 years	Primarily for water projects and veterans' housing	User fees and mortgage payments (no General Fund)
Lease-Payment Bonds	Varies, up to 30 years	Finance capital facilities, particularly corrections and higher education	Annual appropriation, usually General Fund, for lease payments
Revenue Bonds	Varies, up to 30 years	Finance capital facilities that generate revenue streams (such as university dorms)	Typically project-supported (no General Fund)

a Various other borrowing is done which is not state borrowing, but which is used to finance state-related needs. For example, Certificates of Participation (COPs) can be used by private entities or joint powers authorities, and their debt-service can be paid from annually appropriated state lease payments.

State Short-Term Debt Levels and Costs

	Amount Outstanding (12/31/94)	Interest Rate	State Interest Cost
RANs	$3 billion	4.3%	$117 million[a]
RAWs	$4 billion	5.3%	$390 million[b]
Internal borrowing	—[c]	About 5.5%	Minor

[a] Paid in 1994-95; interest cost is net of premium.

[b] Paid in 1995-96. Includes cost of credit enhancement and value of premium in 1994-95.

[c] While there was no internal borrowing at the end of December 1994, small amounts of internal borrowing occur in other months.

Short-Term Borrowing In 1994-95—Governor's Budget Plan

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External Borrowing Activity in 1994-95

☑ **Preexisting RANs and RAWs**

- When 1994-95 started, \$3.2 billion of RAWs were outstanding.
- Of this, \$2 billion was repaid in late July 1994 and \$1.2 billion in late December 1994.

☑ **New RANs and RAWs**

- \$7 billion of new short-term borrowing:
  - — \$4 billion in RAWs, which were sold in July 1994 and will be repaid in April 1996.
  - — \$3 billion in RANs, which were sold in August 1994 and will be repaid in June 1995.

Internal Borrowing Activity in 1994-95

☑ **Borrowing from special funds will not be significant.**

Year-End Position (June 30, 1995)

☑ **At the end of the year, there will be \$4 billion of external borrowing (RAWs) to be repaid.**

☑ **Over \$4.2 billion of unused borrowing ability will be available from internal resources.**

Short-Term Borrowing In 1995-96—Governor's Budget Plan

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External Borrowing Activity in 1995-96

☑ **Preexisting RANs and RAWs**

- $4 billion in RAWs will be outstanding at the start of 1995-96. These will be paid off in April 1996.

☑ **New RANs**

- $2 billion of RANs will be issued in October 1995. These will be paid off in June 1996.

Internal Borrowing Activity in 1995-96

☑ **Internal borrowing will play a much greater role than in 1994-95, ranging monthly between $2.5 billion and $4 billion.**

Year-End Position (June 30, 1996)

☑ **At the end of the year, there will be no external borrowing and $3.4 billion of internal borrowing.**

☑ **$1 billion of unused borrowing ability will remain (all from internal resources). Based on this estimate, the "trigger" would not be activated.**

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Commonly Asked Questions Relating to Short-Term Borrowing

1. **Isn't the $7 billion that we borrowed in 1994 really tantamount to being our budget deficit?**

   No. A budget deficit is when you spend more than you have in resources. Although part of the $7 billion relates to our carryover deficit, it also partly reflects monies temporarily needed to "get us by" until the revenues we collect later in the year come in. It's similar to using a credit card to pay for something in the first week of the month that you pay the bill on later in the month, after you get your paycheck.

2. **How was the $7 billion in short-term borrowing arrived at?**

   In general terms, there were four main factors:

   - Some was needed to temporarily fund the 1993-94 carryover deficit.
   - Several billion were needed for cash-flow management in both 1994-95 and 1995-96.
   - A couple billion was needed for the cash shortfall experienced when the state made off-budget Proposition 98 loans to schools.
   - Some was borrowed to have a "cushion" against contingencies.

3. **If the state didn't rely much on internal borrowing in 1994-95, why did it borrow externally?**

   When you borrow externally, you have to focus on the funds you will need in your "tight" months. The state wouldn't have been able to get by without some external borrowing. As it turns out, however, the state didn't need to borrow the entire $7 billion. This is because when external borrowing was done, the budgetary outlook was less favorable than it is currently.

4. **Why would we ever borrow externally unless we absolutely have to?**

   One reason might be to ensure that you have a sufficient cash "cushion" in case the budget unexpectedly takes a turn for the worse. Because of the time it takes to raise money in the private capital markets, it can make sense to borrow funds ahead of time to protect against contingencies.

5. **Doesn't external borrowing cost us money?**

   Yes. However, if we borrow short-term but do not actually use the funds, we can come out ahead. This is because the federal government lets us borrow externally (within prescribed limits) at tax-exempt rates, but invest any idle proceeds in higher-yielding taxable investments. Most governments borrow externally to the maximum extent permitted.

State Long-Term Debt Levels and Costs

(In Billions)

	Amount Outstanding (12/31/94)	Authorized But Unsold	1994-95 Debt Service Payments
General Obligation Bonds			
General Fund	$14.9	$3.2	$1.9
Self-Liquidating	3.9	0.8	0.5
Lease-Payment Bonds	5.2	1.7	0.3
Revenue Bonds	11.5[a]	—[b]	—[b]

[a] As of June 30, 1993.

[b] Not available.

- ☑ **The majority of state debt service cost is for voter-approved general obligation bonds.**
- ☑ **Debt service on lease-payment bonds has grown significantly in recent years—from $125 million in 1990-91 to $330 million in 1994-95.**
- ☑ **Lease-payment debt will increase to about $500 million in 1997-98 without additional authorizations.**

State Long-Term Debt
Unallocated General Obligation Bonds[a]

(In Millions)

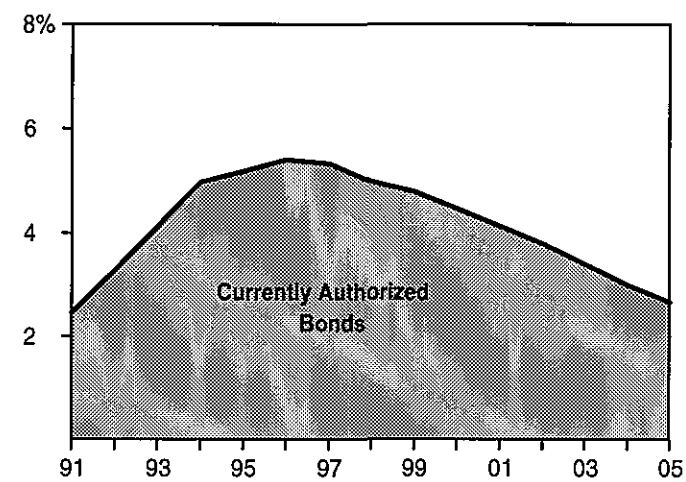
Program	
Transportation (rail programs)	$787
Parks/resources	15
Safe drinking water/clean water/water conservation	92
County correctional facilities	—
State prisons/youth authority	32
K-12	70
Higher Education	46
Libraries	—
Public buildings—seismic upgrading	222
Total	**$1,264**

[a] As of January 1995.

- ☑ **Of the $3.2 billion in unsold general obligation bonds, less than $1.3 billion remains available for allocation to new projects.**

- ☑ **Almost two-thirds of the unallocated total is for transportation (rail programs).**

State Long-Term Debt
Debt Service Ratios



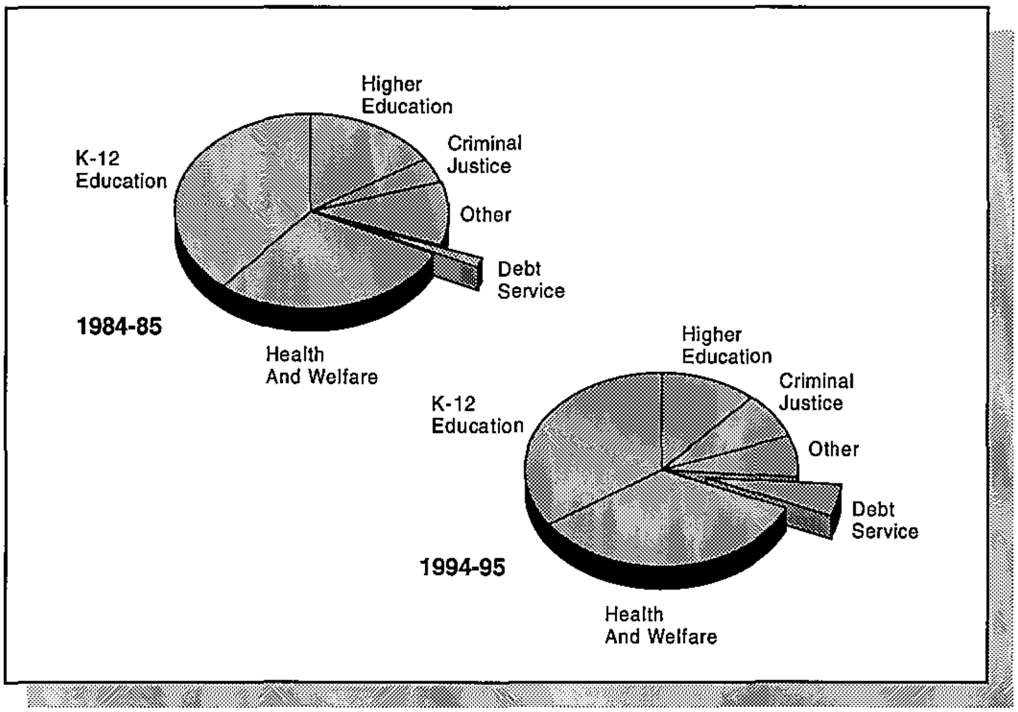
- ☑ The debt service ratio is the cost to pay principal and interest on state bonds as a percentage of state General Fund revenues.

- ☑ The state's debt service ratio has risen in recent years primarily due to increased bond sales, but also due to flat revenue growth.

- ☑ The current debt service ratio is about 5.2 percent.

- ☑ With no additional bond authorizations, the debt service ratio will peak at 5.4 percent in 1995-96 and decline thereafter.

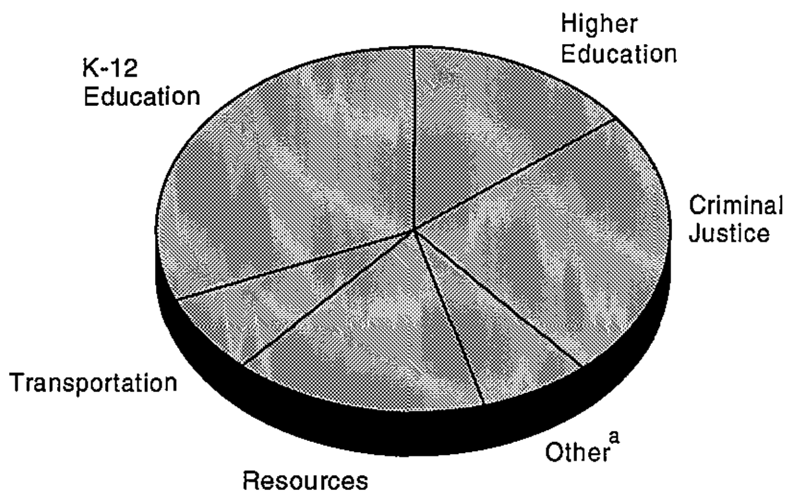
State Long-Term Debt
Share of General Fund Expenditures



- ☑ **In the last ten years, General Fund debt service costs have increased from 1.5 percent to 5.2 percent of total General Fund expenditures.**

- ☑ **In dollar terms, the increase was from $400 million in 1984-85 to $2.2 billion in 1994-95.**

State Long-Term Debt
Debt Service by Program—1994-95



[a] Includes housing, state office buildings, senior citizens' centers, and earthquake safety.

- ☑ **Seventy percent of total debt service is for education and criminal justice capital outlay programs. This includes K-12 schools, higher education, the Department of Corrections, California Youth Authority, and county jail facilities.**

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State Long-Term Debt California Versus Other States

	Net Tax-Supported Debt[a]		
	Percent of Revenues (1993-94)	Percent of 1992 Personal Income	Per Capita
California	4.9%(13)[b]	3.0%(13)[b]	$642(14)[b]
National Average	4.3	3.1	606
Other industrial states			
New York	5.8	6.4	1,509
Illinois	4.4	3.0	654
Ohio	3.6	2.6	461
Texas	2.4	1.2	214
Michigan	2.2	1.5	288
Other western states			
Washington	4.9	5.0	1,034
Nevada	4.6	2.2	443
Utah	3.4	1.6	248
Arizona	2.4	1.6	272
Oregon	1.1	1.2	201

[a] *Source:* Moody's Investment Sources, 1994.
[b] Numerical rank among the 50 states.

- ☑ **California's debt, based on three common measurements, is at or above the national average.**
- ☑ **California's debt ranks in the highest one-third of the states based on the above three measures.**