J00A04

Debt Service Requirements

Maryland Department of Transportation

Operating Budget Data

($ in Thousands)

	FY 02 Actual	FY 03 Working	FY 04 Allowance	Change	% Change Prior Year
Special Funds	$113,505	$134,508	$152,492	$17,984	13.4%
Adjusted Special Funds	**113,505**	**134,508**	**152,492**	**17,984**	**13.4%**
Adjusted Grand Total	**$113,505**	**$134,508**	**$152,492**	**$17,984**	**13.4%**

- Debt service payments increase by $18.0 million.
- The allowance assumes that the department will issue $365 million in Consolidated Transportation bonds in fiscal 2003 and $370 million in bonds in fiscal 2004.

Analysis in Brief

Operating Budget Recommended Actions

		Funds
1.	Add annual language limiting debt outstanding.	
2.	Add language requiring justification for Certificates of Participation.	
3.	Add language requiring nontraditional debt outstanding information.	
4.	Reduce funds for debt service payments.	$ 7,000,000
	Total Reductions	**$ 7,000,000**

Note: Numbers may not sum to total due to rounding.

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Budget Analysis

Program Description

The Maryland Department of Transportation (MDOT) issues 15-year consolidated transportation bonds, which are tax-supported debt. Bond proceeds are usually dedicated for highway construction projects. Revenues from taxes and fees, and other funding sources are combined in the Transportation Trust Fund (TTF) to pay debt service and operating budget requirements and to support the capital program. Debt service on Consolidated Transportation Bonds is payable solely from the TTF.

The department previously issued county transportation bonds, which were considered both State and county debt and counted toward State debt-affordability limits. Chapter 539, Acts of 1993 altered this policy by authorizing the department to continue to issue bonds on behalf of the local jurisdictions without having the local debt apply to State debt-affordability limits. Bonds issued since the 1993 Act only count toward the debt outstanding of the counties. Any remaining debt issued prior to the law still counts toward State debt-affordability limits. It is projected that the remaining debt will be retired in fiscal 2007.

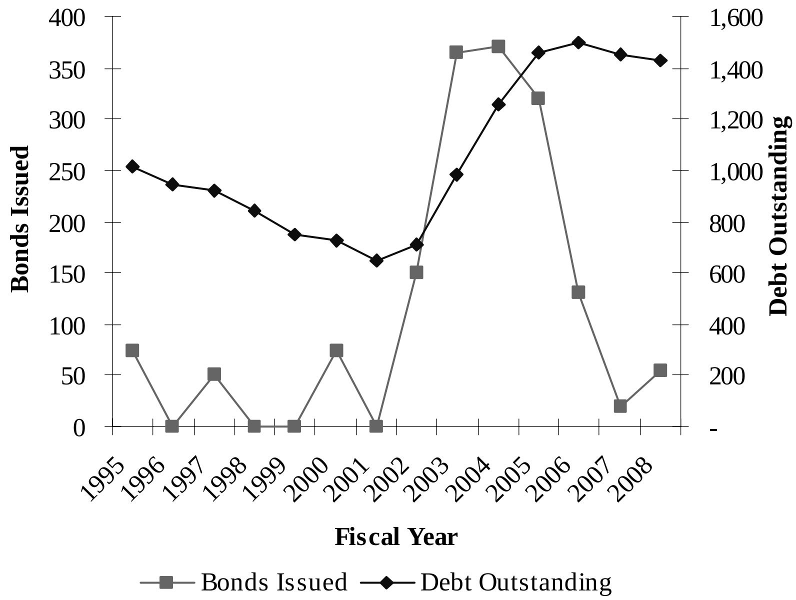
Governor's Proposed Operating Budget

The fiscal 2004 allowance for debt service payments is $152.5 million, including $152.1 million for Consolidated Transportation Bonds and $354,249 for the remaining county bond issues, which count against State debt-affordability limits. Funding for fiscal 2004 increases by $18.0 million, 13.4% more than the fiscal 2003 working appropriation of $134.5 million. The increase in fiscal 2004 is largely due to the new debt issuances projected for calendar 2003 and the timing of debt payment scheduled for previous issues. In addition, due to lower than anticipated debt issuance, MDOT advises that debt service payments in fiscal 2003 will be $6.5 million lower than the working appropriation.

Exhibit 1 shows debt issuance patterns from fiscal 1996 to 2008. At the end of fiscal 1995, debt outstanding reached its peak at $1.015 billion. From fiscal 1989 to 1996, MDOT issued $980 million in new debt. Since fiscal 1996, strong revenue growth has allowed the department to limit total new bond sales to $275 million. MDOT anticipates issuing significantly more debt than in the past beginning in fiscal 2003, in part to offset a planned $300 million transfer from TTF to the State's general fund and allow the department's capital program to remain largely unchanged in fiscal 2003 and 2004. Debt outstanding is projected to be $985 million by the end of fiscal 2003, the highest level of debt outstanding since fiscal 1995. The planned $300 million transfer resulted in the department speeding up planned bond sales from $350 million in fiscal 2003 and $270 million in fiscal 2004 to $365 million and $370 million respectively. This results in an increase of $115 million in bond sales for the current years; however, over the six-year forecast period, there is a minimal $10 million decrease in the total amount of bond sales planned.

Exhibit 1

MDOT Debt Issuance and Debt Outstanding
Fiscal 1995 through 2002 Actual and Fiscal 2003 through 2008 Projected
($ in Millions)



Source: Maryland Department of Transportation, January 2003

In the period fiscal 2004 through 2008, MDOT plans to fund its capital program by issuing bonds totaling $895 million. This will increase debt outstanding to the $1.5 billion statutory limit by the end of fiscal 2005. Debt service expenditures are projected to peak in fiscal 2005 at $180 million.

It should also be noted that the increase in debt outstanding to the statutory maximum of $1.5 billion at the end of the forecast period in fiscal 2008 is in keeping with the department's standard forecasting approach. The forecast typically anticipates a significant increase in reliance on debt in future years to maintain the planned program. Typically the level of debt expected to be sold in the later years of the forecast is reduced when revenue projections come in higher than estimated.

In fiscal 2003, the department plans to issue $365 million in new debt. The first bond sale, $150 million, is scheduled for February 2003. The department also expects to sell $215 million in spring 2003. The January 29, 2003 bond sale also includes the sale of $262.4 million in refunding bonds and will go to pay off debt previously issued. For fiscal 2004, the department advises it anticipates total bond sales of $370 million with issuance of $200 million in fall 2003 and $170 million in spring 2004.

Transportation Bonds Outstanding Meet Legislative and Department Limits

The issuance of transportation debt is limited by two criteria: an outstanding debt limit and a coverage test. By the statute, outstanding debt is limited to $1.5 billion, with the provision that an annual debt ceiling will be set in each budget bill. The debt maximum was raised during the 2002 legislative session from $1.2 to $1.5 billion to reflect the shift of certain revenues dedicated to TTF back to the general fund. These revenues include 55% of the total collected from the sales tax on rental cars, a portion of the security interest filing fees, uninsured motorist penalties, and revenue from vehicle registrations. As of January 2003, MDOT estimates that maximum debt outstanding will be $985 million on June 30, 2003, and $1.253 billion as of June 30, 2004.

The bond revenue coverage tests, established in the department's bond resolutions, mandate that annual net revenues and pledged taxes must equal at least twice (2.0) the maximum future annual debt service. The department has adopted an administrative policy establishing a minimum coverage of 2.5. The net revenues coverage test is the ratio of all prior-year net revenues (excluding federal capital, bond proceeds, and third-party reimbursements) minus prior-year operating expenses, to maximum annual future debt service. The pledged taxes coverage test includes annual net revenues from vehicle excise, motor fuel, and corporate taxes (excluding refunds and all statutory deductions) as a ratio of maximum future annual debt service. As of January 2003, MDOT estimates fiscal 2003 coverage at 4.3 times the maximum annual debt service under the net revenue test and 6.8 times using the pledged tax test. Fiscal 2004 coverage ratios are estimated to be 3.4 under the net revenues test and 6.2 under the pledged tax test.

The department prudently manages its debt through the use of the coverage ratios. Its bond issuances have consistently been rated AA by Moody's and Fitch Ratings – the highest that a State entity typically receives. In addition the department's conservative approach to its coverage ratios, setting an administrative coverage ratio higher than what is required, has also improved its standing with respect to its debt management. By carefully managing outstanding debt, the department has been able to rely on the use of debt in times when TTF revenues are not sufficient to fund all MDOT activities, or as is the case in fiscal 2003 and 2004, to provide $300 million in cash to the State's general fund.

In sum, the General Assembly places limits on the total transportation debt outstanding at the end of the current and subsequent fiscal year. MDOT also limits debt issuance to ensure that transportation debt is managed prudently. Based on current revenue projections, MDOT will be able to manage its debt outstanding within the mandates set by the General Assembly.

Section 3-202 of the Transportation Article requires the General Assembly to adopt annual budget bill language limiting the level of maximum debt outstanding.

Use of Nontransportation Bonds to Fund Transportation Projects Increases

In addition to Consolidated Transportation Bonds, the department issues other nontraditional debt such as certificates of participation (COPs). The department also sells revenue bonds through the Maryland Transportation Authority (MdTA) and has financed the first of at least two projects through the

Maryland Economic Development Corporation (MEDCO). **Exhibit 2** provides details on current nontransportation bonds debt outstanding.

Exhibit 2

Nontraditional Debt Outstanding
Fiscal 2004
($ in Thousands)

Year Issued and Mature	Amount Issued	Principal Outstanding (01/01/03)	FY 04 Payments	Purpose
Certificates of Participation				
1992 to 2010	$20,825	$5,760	$1,200	Refund prior Motor Vehicle Administration (MVA) and State Highway Administration (SHA) traffic facility COPs and support purchase of SHA office buildings.
1993 to 2009	7,820	1,685	190	Refund prior MVA COPs.
1999 to 2026	42,750	29,545	2,586	Expand Piers A and B and a deicing facility at Baltimore/Washington International Airport (BWI).
2000 to 2025	33,000	29,300	3,961	Construct parking garage at Maryland Rail Commuter/Amtrak station near BWI.
Subtotal	**$104,395**	**$66,290**	**$7,937**	
Maryland Transportation Authority Revenue Bonds				
1994 to 2019*	$162,580	$79,220	$0	Construction of an international terminal at BWI, terminal roadway improvements, and Pier C. Revenue bonds are backed by passenger facility charges (PFCs).
2002 to 2027	264,075	264,075	13,243	Construction of Elm Road 8,400 parking garage near BWI. Revenue bonds backed by parking fees collected at BWI.
2002 to 2032	117,345	117,345	9,072	Construction of a central rental car facility at BWI. Revenue bonds backed by customer facility charge of $3.00.
Subtotal	**$544,000**	**$460,640**	**$22,315**	

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Year Issued and Mature	Amount Issued	Principal Outstanding (01/01/03)	FY 04 Payments	Purpose
Maryland Economic Development Corporation				
2002 to 2022	$36,000	$36,000	$2,901	Construction of a new MDOT headquarters building due to demolition of existing building for expansion at BWI.
Subtotal	**$36,000**	**$36,000**	**$2,901**	
Nontraditional Debt				
Total	**$684,395**	**$562,930**	**$33,153**	

Note: Numbers may not sum due to rounding.
*MDOT plans to defease these bonds in fiscal 2003 and redeem on June 1, 2004.
Source: Maryland Department of Transportation, January 2003

MDOT advises that during fiscal 2003 it intends to call two outstanding COPs series. Both the 1992 and 1993 series have higher than prevailing interest rates and by calling this debt now, MDOT will save $1,126,280 in interest costs. Due to lower than planned consolidated transportation bond issuance in previous years the department has the resources to retire this debt at this time. As a result recommendations to delete fiscal 2004 funds for COPs debt service payments in the State Highway Administration and the Motor Vehicle Administration budget will be made.

During fiscal 2002 and 2003, MDOT issued $417.4 million in nontraditional debt. This includes revenue bonds for new parking facilities and a consolidated rental car facility at BWI. In addition a replacement headquarters building, necessary due to expansion projects at BWI, was financed through MEDCO. Debt service payments for the parking garage and rental car facility are met by dedicated revenue sources. Debt service for the MEDCO bonds is funded through the Secretary's Office operating budget.

Future Nontraditional Debt Issuance Planned

During fiscal 2004, MDOT plans two nontraditional debt issuances for a total of $280 million. In March 2003, MDOT intends to issue $230 million for construction of an expanded terminal building and Piers A and B at BWI. A memorandum of understanding has been signed with Southwest Airlines for the use of the space. Debt service in fiscal 2006, once construction is complete, will be met using lease revenue paid by airline and concession tenants. In June 2003, MDOT plans to sell $50.0 million through the MdTA to construct roadway, terminal curbside pedestrian access/circulation, apron/taxiway and expansion of Piers A and B.

In its 2002 report, the Spending Affordability Committee noted the substantial growth in nontraditional debt issued by State agencies and independent authorities. The committee's concern was that the increased use of nontraditional bonds is not subject to the same oversight constraints as traditional State debt, and its growth places increased pressure on the pledged revenues to cover the debt service. The committee urged the Capital Debt Affordability Committee to include non-tax supported debt in its annual review of State debt outstanding.

Recommendations

Beginning with the fiscal 2002 budget, the General Assembly adopted budget bill language to establish an oversight process for the issuance of COPs. **To continue prudent financial management and General Assembly oversight of long-term liabilities, the Department of Legislative Services recommends adoption of budget bill language limiting the outstanding and unpaid principal balance of COPs. In addition, budget bill language is recommended requiring that the department include nontraditional debt outstanding information with its annual forecast. In addition, the department should submit to the budget committees debt outstanding for nontraditional debt for fiscal 1999 through 2004.**

Operating Budget Recommended Actions

1. Add the following language:

   Consolidated Transportation Bonds may be issued in any amount provided that the aggregate outstanding and unpaid principal balance of these bonds and bonds of prior issues shall not exceed $ as of June 30, 2004. Provided, however, that in addition to the limit established under this provision, the department may increase its debt outstanding by not more than $15,000,000, so long as (1) notice stating the specific reason for the additional debt requirement is provided to the budget committees; and (2) the budget committees have 45 days to review and comment on the proposal before publication of a preliminary official statement including the debt.

   Explanation: Section 3-202 of the Transportation Article requires the General Assembly to establish the maximum debt outstanding each year in the budget bill. The level will be based on outstanding debt as of June 30, 2003, plus projected debt issued during fiscal 2004 in support of the transportation capital program. The language further provides that the Maryland Department of Transportation may request the budget committees to increase the level of maximum debt outstanding by $15 million during the fiscal year, upon notification to the budget committees of the specific reason for the additional debt requirement.

Information Request	**Author**	**Due Date**
Justification for $15 million increase in debt outstanding	MDOT	45 days prior to publication of a preliminary official statement

2. Add the following language:

   Certificates of Participation (COPs) may be issued in any amount provided that the aggregate outstanding and unpaid principal balance of these financial instruments and prior issues shall not exceed $ as of June 30, 2004. Provided, however, that in addition to the limit established under this provision, the department may increase the outstanding unpaid and principal balance associated with these financial instruments so long as (1) notice stating the specific reason for the additional issuance is provided to the budget committees; and (2) the budget committees have 45 days to review and comment on the proposal before publication of a preliminary official statement.

   Explanation: The language formalizes a legislative oversight process that the department must comply with regarding the issuance of COPs. The information provided to the committees will include the amount to be issued; a description of the project to be financed; and identification of a revenue stream, payback period, and financial assurances that would be incorporated into the deal.

Information Request	**Author**	**Due Date**
Justification for new issuance of COPs	MDOT	45 days prior to publication of preliminary official statement

3. Add the following language:

<u>The Maryland Department of Transportation (MDOT) shall submit with its annual September and January financial forecast information on anticipated nontraditional debt outstanding as of June 30 of each year. Nontraditional debt outstanding is defined as any debt instrument that is not consolidated transportation bonds and includes, but is not limited to, certificates of participation, debt backed by customer facility charges, passenger facility charges, or other revenues, and debt issued by the Maryland Economic Development Corporation or any other third party on behalf of MDOT. In addition MDOT shall submit historical nontraditional debt outstanding information as of June 30 of each year for the period fiscal 1999 through 2004 by July 1, 2003.</u>

Explanation: The budget committees are interested in monitoring the unconstrained use of nontraditional debt by MDOT. The information requested provides the budget committees with additional information on the usage of nontraditional debt.

Information Request	**Author**	**Due Date**
Nontraditional debt outstanding	MDOT	September forecast January forecast
Nontraditional debt outstanding information for fiscal 1999 through 2004.	MDOT	July 1, 2003

	Amount <u>Reduction</u>	
4. Reduce funds for debt service payments. Due to interest savings from the sale of refunding bonds totaling $262.4 million in fiscal 2003, the Maryland Department of Transportation is estimating that funds necessary to pay debt service in fiscal 2004 will total $145,491,737, an amount that is $7 million less than the current fiscal 2004 allowance. This reduction simply reduces the amount available for debt service payments based on the department's latest financial forecast.	$ 7,000,000	SF
Total Special Fund Reductions	**$ 7,000,000**	

Appendix 1

Current and Prior Year Operating Budgets

Current and Prior Year Operating Budgets

MDOT - Debt Service Requirements

($ in Thousands)

	General Fund	Special Fund	Federal Fund	Reimb. Fund	Total
Fiscal 2002					
Legislative Appropriation	$0	$117,241	$0	$0	$117,241
Deficiency Appropriation	0	0	0	0	0
Budget Amendments	0	0	0	0	0
Reversions and Cancellations	0	-3,735	0	0	-3,735
Actual Expenditures	**$0**	**$113,506**	**$0**	**$0**	**$113,506**
Fiscal 2003					
Legislative Appropriation	$0	$134,507	$0	$0	$134,507
Budget Amendments	0	0	0	0	0
Working Appropriation	**$0**	**$134,507**	**$0**	**$0**	**$134,507**

Note: Numbers may not sum to total due to rounding.

Major Changes in Current and Prior Year Appropriations

The fiscal 2002 debt service expenditures totaled approximately $113.5 million, which is $3.7 million less than the legislative appropriation. The department cancelled $3.7 million as the department did not proceed with planned a bond sale during fiscal 2001 for which debt service payments would have been necessary.

Object/Fund Difference Report
MDOT - Debt Service Requirements

Object/Fund	FY 02 Actual	FY 03 Working Appropriation	FY 04 Allowance	FY 03 – FY 04 Amount Change	Percent Change
Objects					
13 Fixed Charges	$ 113,505,355	$ 134,507,780	$ 152,491,737	$ 17,983,957	13.4%
Total Objects	**$ 113,505,355**	**$ 134,507,780**	**$ 152,491,737**	**$ 17,983,957**	**13.4%**
Funds					
03 Special Fund	$ 113,505,355	$ 134,507,780	$ 152,491,737	$ 17,983,957	13.4%
Total Funds	**$ 113,505,355**	**$ 134,507,780**	**$ 152,491,737**	**$ 17,983,957**	**13.4%**

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