Capital Debt Affordability Committee
Treasurer Nancy K. Kopp, Chair

Agenda

October 19, 2020
1:00 PM

1) **Treasurer's Opening Comments**

2) **Changes to Guidance on State's Use of Bond Premium**
Christian Lund, Director of Debt Management, State Treasurer's Office

3) **Affordability Analysis**
Christian Lund, Director of Debt Management, State Treasurer's Office

4) **Committee Discussion and Voting Session on the 2020 Capital Debt Affordability Committee Recommendations**

   - *General Obligation Bond Authorization and Planning Assumptions:*
     Recommendation of the amount of new State debt that may prudently be authorized for fiscal year 2022, and planning assumptions for the total amount of new State debt for future fiscal years.

   - *Academic Facilities Bonds Authorization:*
     Recommendation of the amount of new bonds for academic facilities for fiscal year 2022 by the University System of Maryland, Morgan State University, St. Mary's College of Maryland and the Baltimore City Community College.

State of Maryland's
Use of Bond Premium

October 19, 2020

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Introduction

- A recent change in guidance from the State's bond counsel will impact the way the State uses bond premium attained from its General Obligation bond sales

- No action is needed by CDAC – this presentation is for informational purposes only

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Background:
Allowable Uses of Bond Proceeds*

- Federal tax law restricts expenditures to:
  - Capital projects
  - Certain interest costs
  - *De minimus* exceptions, i.e. cost of issuance and other directly attributable costs not more than 5% of total proceeds
  - Certain other expenditures

- State law requires that:
  - Normal bond proceeds must be used to pay for capital projects
  - Bond premium must be used to pay for debt service (unless specific authorization is given to use it for a different purpose)

*Bond proceeds include both normal bond proceeds and any bond premium attained.

Background: Bond Counsel and Tax Certificates

- Though most of the restrictions on use of proceeds are well-defined, the statute governing which interest costs are allowed is murky and have never been tested in court
  - In the absence of clear guidance, individual legal firms (**bond counsels**) have made their own interpretations of the statute
  - Opinions differ significantly from bond counsel to bond counsel

- As part of each bond sale, the State's bond counsel provides a **tax certificate**, portions of which:
  - Describe the expected way in which bond premium will be used
  - Opine that the expected use of premium complies with applicable federal and state law

Change in Bond Counsel's Tax Certificate

- Earlier this year, the State's bond counsel changed its interpretation of what interest costs may be paid using bond premium

- This change in guidance is closer to the consensus view among bond counsels

- This change impacts the allowable use of premium from the most recent bond sale as well as future State bond sales

Change in Bond Counsel’s Tax Certificate

- In the past, bond counsel issued tax certificates to the State allowing it to use premium to pay:
  - Up to three years of interest on the current bond issue
  - Interest payments for any other bond issue occurring within one year of the sale date of the current issue

- Beginning with the 2020 1st Series, bond counsel changed its interpretation of the federal statute

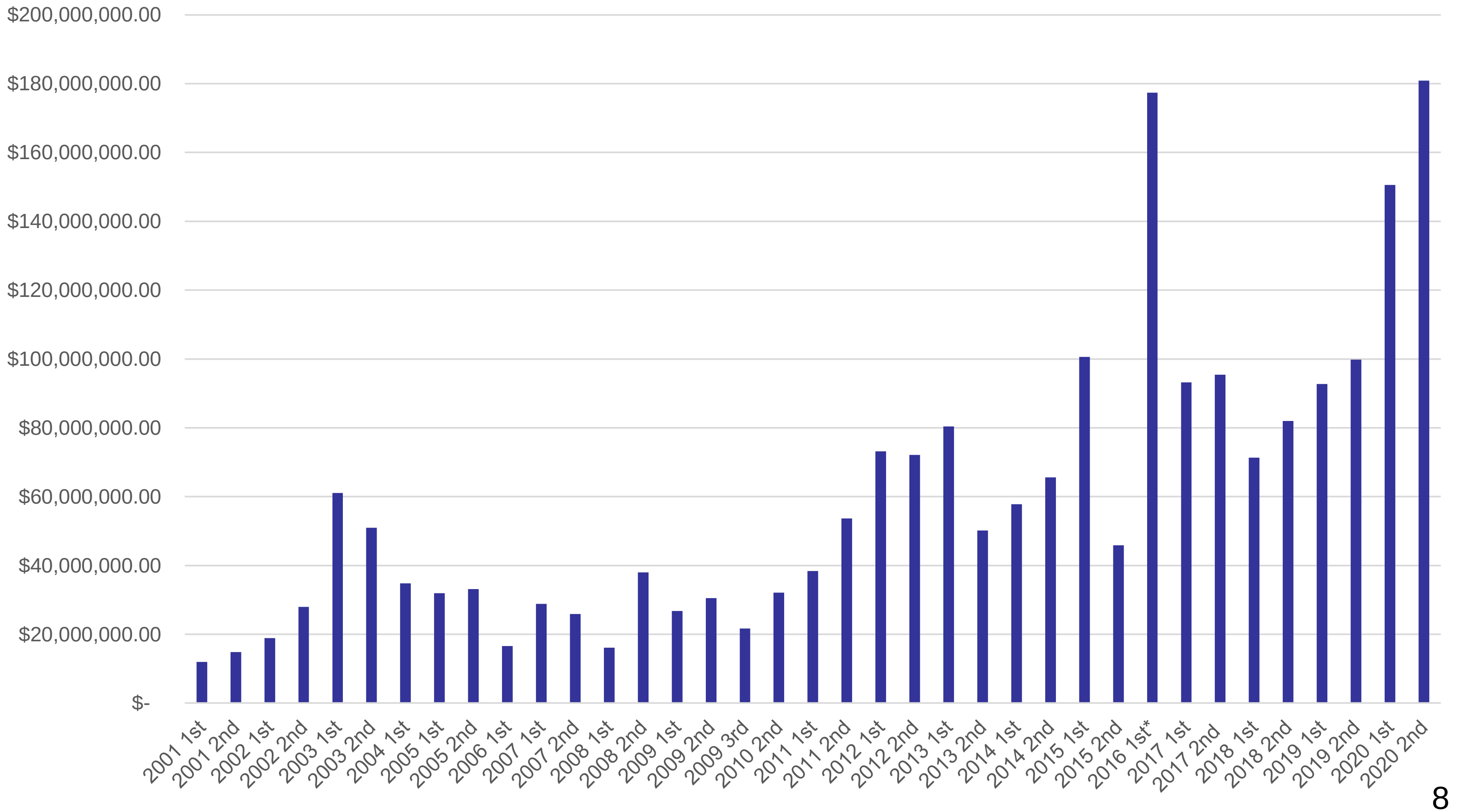
- Bond counsel’s tax certificate no longer allows the State to use premium to pay interest on other bond issues (only the current issue)

Impact of Changes

- The State needs to authorize additional premium-funded capital projects so it can allocate $31 million in premium attained during the 2020 2nd Series

- Moving forward, bond premium in excess of three years of interest costs needs to be applied to projects or used to resize the bond sale (for comparison, three years of interest payments for the 2020 2nd Series totaled $67 million)

Bond Premium Attainment
2001 1st Series – 2020 2nd Series



Not All Bad News

- The State will still be able to put excess premium to good use:
  - **Capital projects**: the State may either authorize additional infrastructure investments to be paid for with bond premium, or pay for already-planned projects with premium rather than issuing debt
  - **Resizing bond sales**: the State may use the premium to resize bond sales, which will lead to decreased debt outstanding and debt service

Next Steps

- No action by CDAC is needed.

- Moving forward, the State will need to do the following:
  - Only allocate an amount equal to three years of interest payments on the current new money issue to bond premium, in accordance with bond counsel's most recent guidance.
  - Update SF&P § 8-132 and prior MCCBLs to give the State more flexibility with use of bond premium.
  - Begin regular appropriation for arbitrage rebate payments to federal government.

- STO, DBM, DLS, and the Comptroller's Office are working together to address these issues.

Questions?

Christian Lund

Director of Debt Management

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2020 Affordability Analysis

Presented to the Capital Debt Affordability Committee

Christian Lund
Director of Debt Management
Maryland State Treasurer's Office

October 19, 2020

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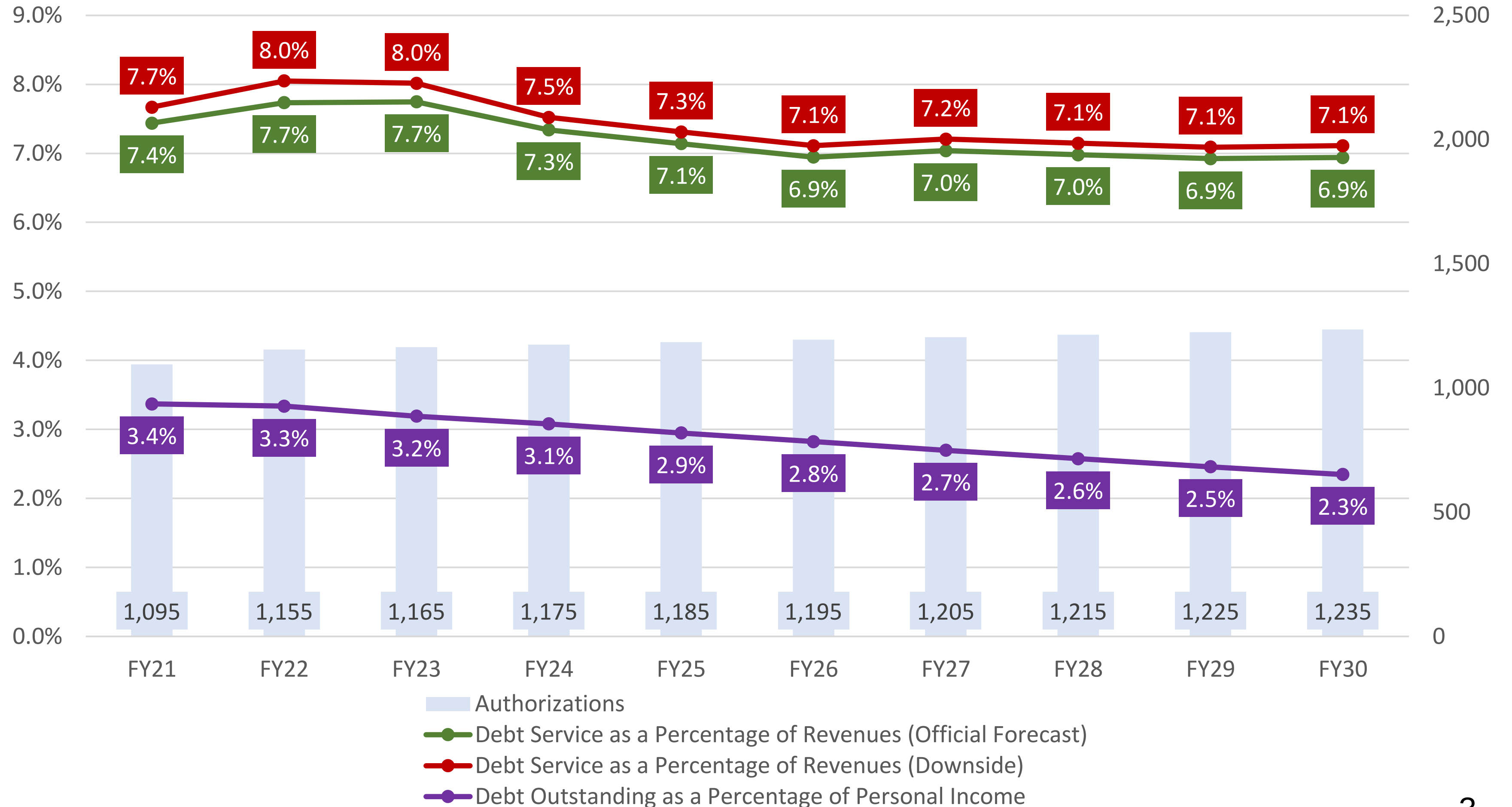
CDAC Authorization Scenarios

($ in millions)

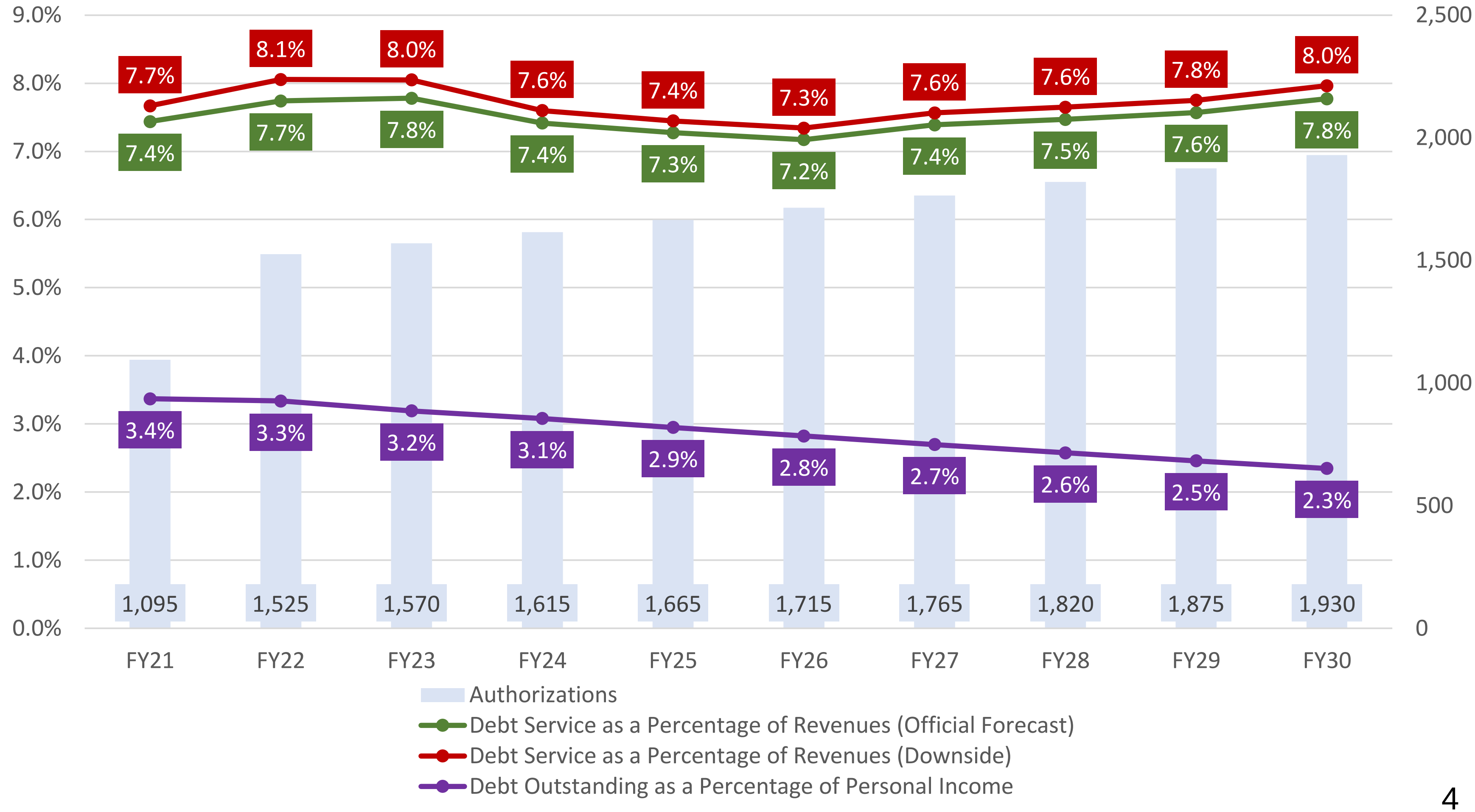
	Scenario 1: Governor's Capital Program	**Scenario 2: Traditional CDAC**
FY	Authorization	Authorization
2021 (actual)	1,095	1,095
2022	1,155	1,525
2023	1,165	1,570
2024	1,175	1,615
2025	1,185	1,665
2026	1,195	1,715
2027	1,205	1,765
2028	1,215	1,820
2029	1,225	1,875
2030	1,235	1,930

Benchmarks: Governor's Capital Plan



All $ millions. Estimates as of 10/16/2020. Tentative and subject to change.

Benchmarks: Traditional CDAC



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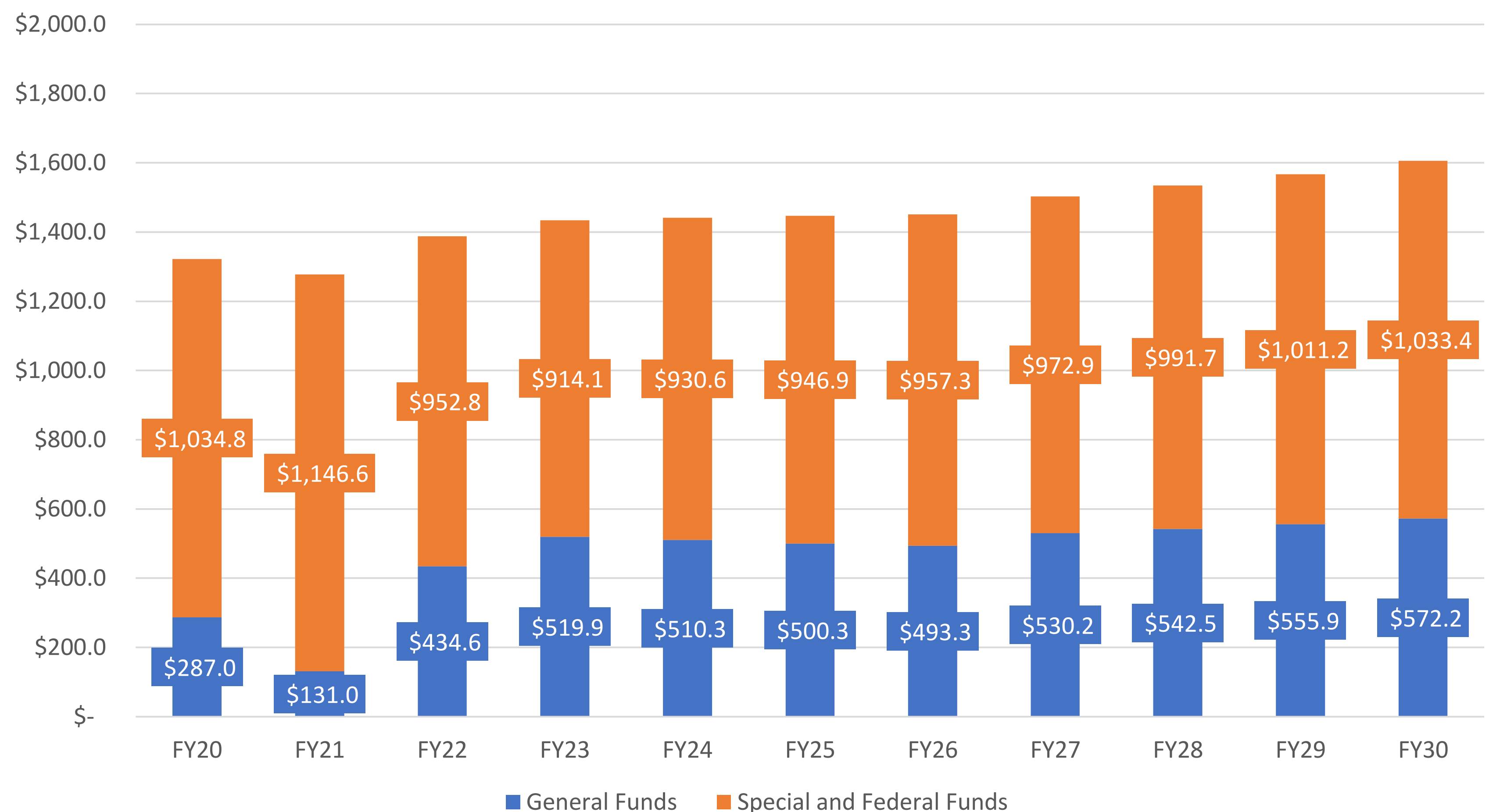
Debt Service Projection: Governor's Capital Plan



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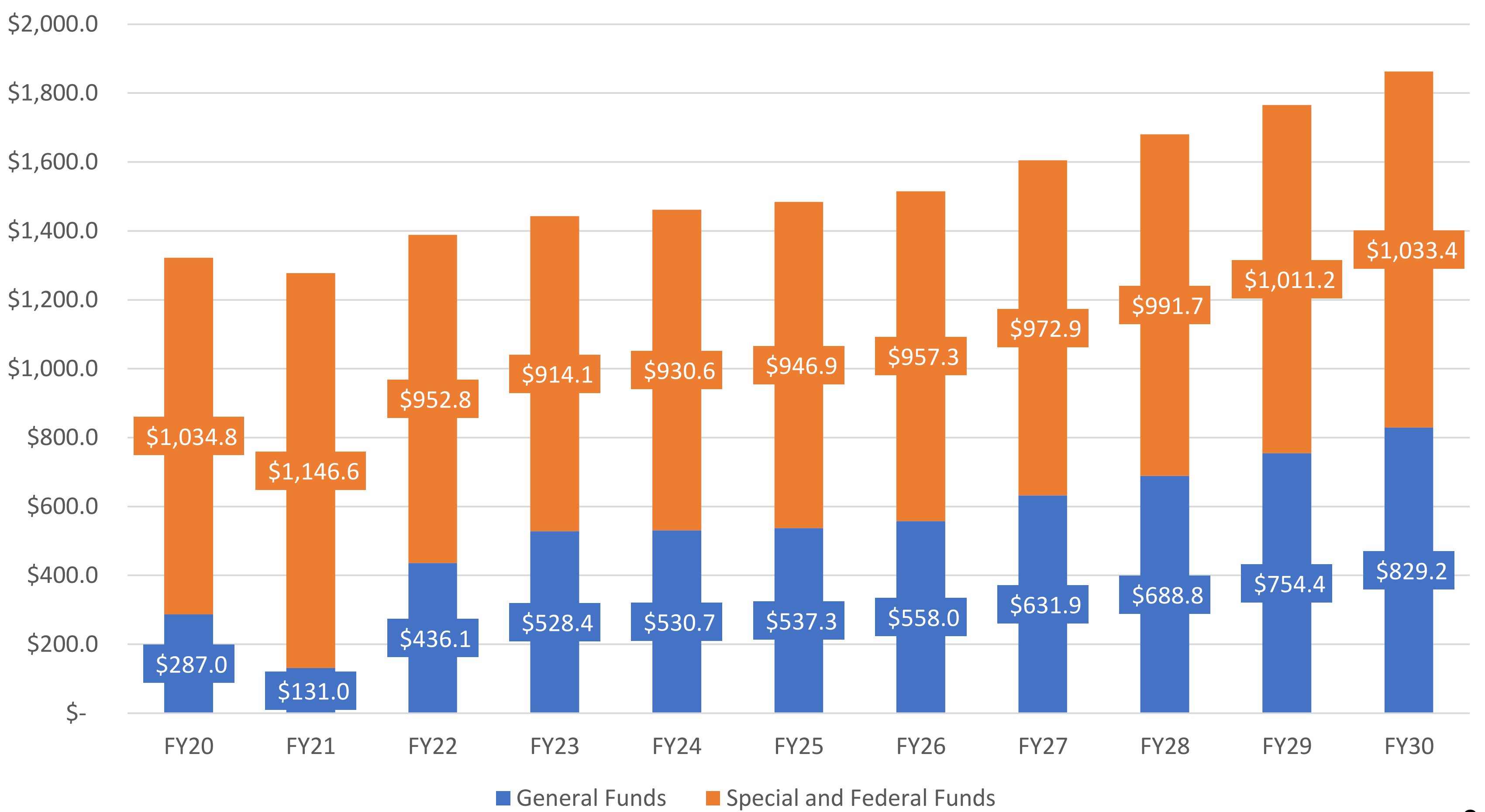
Debt Service Projection: Traditional CDAC



All $ millions. Estimates as of 10/16/2020. Tentative and subject to change.

Recommendation of Amount of New General Obligation Bonds for Fiscal Year 2022

CDAC General Obligation Bond Authorization

- CDAC needs to vote on its recommendation for a General Obligation Bond authorization for FY 2022.
- CDAC only votes on the upcoming fiscal year's authorization (FY 2022). Assumed authorizations for FY 2023 – 2026 are for planning purposes only and subject to change.

Recommendation of Amount of New Bonds for Academic Facilities for Fiscal Year 2022

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Amount of new bonds for academic facilities for fiscal year 2022 requested by institution:

University System of Maryland:	$30.0 million
Morgan State University:	$0.0
Baltimore City Community College:	$0.0
St. Mary's College of Maryland:	$0.0
Total Requested	$30.0 million