CALIFORNIA
DEBT
ADVISORY
COMMISSION

The Use of General Obligation Bonds by the State of California

THE USE OF GENERAL OBLIGATION BONDS

BY THE

STATE OF CALIFORNIA

September 9, 1987

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The State of California is a strong municipal credit and has been an active issuer of general obligation bonds. The State is currently rated AAA by two of the three major credit rating agencies and Aa by the third. With $8,028,550,000 in outstanding State general obligation debt as of June 30, 1987, California has more outstanding debt than any other state.

This report, prepared by the California Debt Advisory Commission, examines the use of general obligation bonds by the State of California. The report was prepared in response to concerns and questions raised by Commission members and others regarding the State's ability to assume additional general obligation debt.

It is hoped that the information provided in this report will assist State policy makers and the public in its ongoing discussions regarding California's willingness and ability, or capacity, to absorb additional general obligation debt.

Sincerely,

Elizabeth M. Whitney

ELIZABETH M. WHITNEY
Acting State Treasurer
Chairman, California Debt Advisory Commission

CALIFORNIA DEBT ADVISORY COMMISSION

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BY THE STATE OF CALIFORNIA

I. INTRODUCTION

This report examines the use of general obligation bonds by the State of California. Its purpose is to provide policy makers with an overview of how California has approached the promise to repay debt as represented by a general obligation bond.

The staff of the California Debt Advisory Commission undertook this report in response to concerns and questions raised by Commission members and others regarding the State's ability to assume additional general obligation bond debt. Staff has reviewed various reports, analyses, and data sources in an attempt to provide a summary of the background and context in which the State has initiated, approved and implemented general obligation bond programs.

It is hoped that the information provided in this report will assist State policy makers and the public in ongoing discussions about the State's willingness and ability, or capacity, to absorb additional general obligation debt.

It is important to emphasize that this report focuses on general obligation debt rather than revenue bond or lease revenue debt, or other types of debt. As such, it will address factors specific to general obligation debt analysis such as personal income levels, as opposed to the financial feasibility of a specific project.

Following this introduction, Section II briefly summarizes this report and suggests issues for consideration by policy makers regarding the State's use of general obligation debt. Section III presents an overview of State general obligation bonds. Section IV describes recent discussions among California policy makers concerning the use of State general obligation debt. Section V profiles the approach of each of the three major credit rating agencies in analyzing state general obligation debt. Lastly, Section VI reports on the use of general obligation debt in other selected states.

II. SUMMARY

The following summarizes the principal findings of this report.

1. The State of California is a strong municipal credit and has been an active issuer of general obligation bonds. The State is currently rated AAA by two of the three major credit rating agencies and Aa by the third. With $8,028,550,000 in outstanding State general obligation debt as of June 30, 1987, California has more outstanding general obligation debt than any other state.

2. The California Constitution and California State law set forth a specific process for the approval and issuance of State general obligation bonds. While these provisions do not limit the dollar amount of State general obligation debt which may be issued or outstanding or specify the purposes for which such debt may be issued, they assure the development of a consensus by requiring a majority vote of the people as well as a consistency in the manner in which the State general obligation bond programs are established.

3. Eighty percent of all State general obligation measures considered by the voters in the 48 general obligation bond elections since 1900 have been approved. Prior to 1960, 71.0 percent of the approved measures received at least 65.0 percent of the votes cast. Since 1960, only 38.0 percent of the measures approved received more than 65.0 percent of the vote.

4. General obligation bonds have been used by the State of California to finance a variety of programs ranging from grants to local agencies for water and wastewater system improvements to State and local park acquisition to county jail and State prison construction. However, the purposes for which the State of California issues general obligation bonds are generally consistent with the activities of other states.

5. The largest number of State general obligation measures considered by the voters on one ballot was six at the November 6, 1984 election and the November 3, 1914 election. The greatest aggregate dollar amount considered was $1,800,000,000 at the November 4, 1986 general election. The single largest issue was $1,750,000,000 approved November 8, 1960 for the State Water Project.

6. There is $5,205,000,000 in State general obligation bonds which are currently authorized but have not yet been issued. Of this total, 65.2 percent or $3,395,000,000 was approved for eight bond programs by the voters in the elections held in 1986. Issuance of these bonds has been hampered by provisions of the federal Tax Reform Act of 1986. Additionally, there are ten other programs in which more than 40 percent of the original amount authorized is unissued.

7. Pressures to fund expenditures through voter-approved debt such as general obligation bonds have increased--with the Gann expenditures limit being a contributing factor.

Legislation proposing voter-approval of $14,495,000,000 in additional State general obligation bonds is pending before the Legislature as this report is written. (This total includes duplicate amounts for certain programs proposed in both Assembly and Senate bills.) The single largest measures proposed are for State transportation improvements. These two measures propose bond authorizations of $1,000,000,000 and $1,500,000,000. The State of California has not considered the approval of general obligation bonds for transportation programs since 1920.

Other measures would provide assistance for housing, K-12 schools, prisons, water quality and conservation, higher education facilities, veterans housing, seismic safety, libraries, law enforcement training, child care facilities, and the proposed superconducting super collider.

Additionally, an initiative proposing the authorization of $776,000,000 in State general obligation bonds is being circulated.

8. Policy making with regard to the use of general obligation bonds by the State of California has been principally developed by the State Treasurer's Office, the Governor's Administration, and the California Legislature. Often, these policy considerations have been expressed in the context of which bills and how much total bond authorization should be put to a vote of the people.

Although no formal policy guidelines have been implemented to assist in these deliberations, this ad hoc process has worked reasonably well with prudence dictating that reasonable amounts of proposed indebtedness for programs which benefit the general public be dominant considerations. The State's strong general obligation bond ratings and low debt ratios support the view that the informal process used by the State has worked reasonably well to date.

The ad hoc nature of the process underscores the need for State policy makers to pay close attention to the use of State general obligation debt. This requires balancing the safe-guarding of the State's credit rating; a commitment to make adequate investment in State programs, facilities, and infrastructure; and the protection of future Californians from excessive bonded indebtedness.

9. Although no formal written policy has been developed to specify the type of programs or amount of indebtedness for California's general obligation bond programs, certain debt limits have been discussed by State policy makers in the last few years.

Notably, the credit rating agencies consider strict, formal debt limits as artificial constraints which could severely restrict a state's ability to respond to an emergency or to make necessary ongoing improvements in its infrastructure.

10. Three major credit rating agencies currently rate municipal debt. All three focus on four rating factors: economic, financial, debt, and administrative. The ratings are informed, subjective judgments of the creditworthiness of a particular issue, not recommendations to buy or sell certain municipal debt. The presence of different ratings by the credit rating agencies on the same issue underscore the fact that the ratings are not assigned through a simple (or even complex) mathematical calculation. Different emphases on the above four factors may result in different ratings.

11. California's general obligation bonds are currently rated AAA by Standard & Poor's Corporation and Fitch Investors Service, Inc. (AAA is the highest possible rating.) Moody's Investors Services, Inc. currently rates California's general obligation bonds Aa.

The strengths cited by the rating agencies in their analyses of California's general obligation debt include a strong economy, low debt ratios, stable financial operations, and a comfortable reserve in the State's budget. However, all three agencies acknowledge the potential impact of the initiative process in California and express varying levels of concern about the effect of such initiatives on the State's financial well-being.

12. California compares favorably to the other 49 states in terms of debt indicators. Moody's medians place California at rank 32 in net tax-supported debt per capita and rank 36 in net tax-supported debt as a percentage of personal income.

Of the nine Standard & Poor's AAA-rated states, California ranks 7th in terms of debt service as a percent of total expenditures. The only two AAA-rated states with lower debt burdens are Missouri and Virginia--each with less than $700,000,000 in outstanding gross State debt.

13. California is among the 23 states which require voter-approval of state general obligation bonds. Five states are not currently authorized to issue general obligation bonds.

14. California is one of eight states with no direct or indirect dollar limits on the amount of general obligation debt which may be issued or outstanding. Thirty-four states have statutory or constitutional limits on either the amount of state general obligation debt which may be outstanding or the amount of debt service which may be incurred.

15. California, like the majority of states, has no written debt management policies. However, like most states, California policy makers monitor the effects of proposed general obligation debt on standard debt indicators such as the ratios of debt to population and debt to personal income and assess the impact of proposed general obligation programs on the State's fiscal resources.

16. An analysis of the use of general obligation bond proceeds for 40 of 50 states during the last four years, indicates that state general obligation bonds have been issued for purposes such as cash-flow, multiple capital improvements, transportation, and housing.

III. OVERVIEW OF CALIFORNIA GENERAL OBLIGATION BONDS

This section defines a State general obligation bond, discusses the legal authority for State general obligation bonds, outlines the process for approval for this type of debt, presents a history of all State general obligation bond measures presented to the voters since 1900, briefly discusses the general obligation bond measures which have been approved by the voters but which have not yet been issued, and summarizes the State general obligation bond measures currently pending in the California Legislature.

A. DEFINITION OF STATE GENERAL OBLIGATION DEBT

General obligation bonds are generally defined as governmental debt which is repaid from general fund revenues and secured by the full faith, credit, and taxing power of the issuer. Under the State Constitution, debt service on outstanding State general obligation bonds is the second charge to the general fund after the support of the public school system including institutions of higher learning.

The State also utilizes other types of debt instruments such as certificates of participation, public lease revenue bonds, and revenue bonds. Certificates of participation and public lease revenue bonds are distinguished from general obligation bonds in that they are not secured by the full faith, credit, and taxing power of the issuer. They are similar in that they may be secured directly or indirectly by State general fund revenues. For this reason, certificates of participation and lease revenue debt are often included in figures for total general fund/tax-supported debt by rating agencies. (As of June 30, 1987, $1,231,375,000 has been issued in notes or bonds for which a long-term lease arrangement with a State agency is the security for repayment. As such, appropriations in the State's budget provide the lease payments which flow to the bond holders.)

In contrast, revenue bonds are repaid by charges, fees, or other revenues collected from users or beneficiaries of the financed project or program and are not general obligations of the State.

For purposes of this report, general obligation bonds are classified into two categories: non self-liquidating and self-liquidating.

Most of California's general obligation bond programs are non self-liquidating. That is, although a general obligation bond program may receive revenues that may be used to retire the debt, the bonds are secured by an unqualified pledge of the full faith, credit, and taxing power of the State of California. For example, under the Safe Drinking Water Bond program, loans may be made to water districts for system improvements. However, the underlying security for repayment of the bonds is the State's general fund and its general obligation pledge, regardless of the amount of funds received as loan repayments.

Self-liquidating bonds are also known as "enterprise fund" general obligation bonds. These bonds derive revenue from payments of beneficiaries which is then used to retire the debt. For example, revenues derived from payments by local water agencies under water supply contracts from the State Water Project are used to retire the bonds which fund the Project and related facilities. Enterprise funds reimburse the State's general fund for debt service provided on their behalf. Although these bonds are also secured by an unqualified pledge of the State's full faith, credit, and taxing power, these financing programs are structured to ensure minimal, if any, actual payment (without reimbursement) of debt service by the general fund.

The designation of self-liquidating or non self-liquidating is not a legal matter, but is used for budget and policy planning. All State general obligation bonds legally have the same full faith, credit, and taxing power backing.

As of June 30, 1987, the amount of outstanding general obligation bonds totalled $8,028,550,000, with an additional $5,205,000,000 authorized but unissued. Table 1 on pages 8 and 9 lists the 39 authorized general obligation bond programs and presents the current status of each program's authorized, outstanding and unissued amounts. Of the total, 34 programs are non self-liquidating and five are self-liquidating. The five self-liquidating bond programs are California Water Resources Development bonds, Harbor Development bonds, San Francisco Harbor Improvement bonds, State School Building Aid bonds, and Veterans Housing bonds. Of these five, only two programs (water resources development and veterans housing) are active.

B. LEGAL AUTHORITY PERTAINING TO STATE GENERAL OBLIGATION BONDS

Constitutional authority for the use of general obligation bonds by the State is found in Article XVI of the State Constitution which is summarized in Table 2 on page 10. Among other provisions, this article specifies that a vote of the people is required to incur indebtedness.

In addition, the principal statutes dealing with general obligation bonds are found in Division 4, Part 3 of the Government Code beginning with Section 16650. This part is commonly known as the General Obligation Bond Law and provides the procedures to be followed in the sale, issuance, and repayment of every general obligation bond issue. This section is incorporated by reference in authorizing statutes for specific general obligation bond programs. These provisions are summarized on Table 3 on page 11.

C. PROCESS FOR APPROVAL OF STATE GENERAL OBLIGATION BONDS

State general obligation bonds generally begin in the Legislature, in either the Senate or the Assembly. However, under Article II, Section 8, of the California Constitution, State general obligation bonds may also be proposed by the people of the State through the initiative process.

Table 1

SUMMARY OF AUTHORIZED AND OUTSTANDING STATE GENERAL OBLIGATION BOND PROGRAMS AS OF JUNE 30, 1987

Bond Authorization	Amount Authorized	Amount Outstanding	Amount Unissued
NON SELF-LIQUIDATING (General Fund Bonds)			
California Clean Water Bond Act of 1970	$250,000,000	$84,500,000	$10,000,000
California Clean Water Bond Act of 1974	250,000,000	139,750,000	20,000,000
California Clean Water Bond Act of 1984	325,000,000	23,750,000	300,000,000
California Clean Water and Water Conservation Bond Law of 1978	375,000,000	252,710,000	45,000,000
California Park and Recreational Facilities Act of 1984	370,000,000	89,000,000	275,000,000
Community College Construction Bond Act of 1972	160,000,000	63,250,000	----------
Community Parklands Act of 1986	100,000,000	----------	100,000,000
County Correctional Facility Capital Expenditure Bond Act of 1986	495,000,000	----------	495,000,000
County Jail Capital Expenditure Bond Act of 1981	280,000,000	137,475,000	130,000,000
County Jail Capital Expenditure Bond Act of 1984	250,000,000	117,500,000	125,000,000
First Time Home Buyers Bond Act of 1982	200,000,000	9,350,000	185,000,000
Fish and Wildlife Habitat Enhancement Act of 1984	85,000,000	27,500,000	55,000,000
Hazardous Substance Cleanup Bond Act of 1984	100,000,000	47,500,000	50,000,000
Health Science Facilities Bond Act of 1971	155,900,000	73,995,000	----------
Higher Education Facilities Bond Act of 1986	400,000,000	----------	400,000,000
Junior College Construction Program Bond Bond Act of 1968	65,000,000	13,300,000	----------
Lake Tahoe Acquisitions Bond Act	85,000,000	28,000,000	55,000,000
New Prison Construction Bond Act of 1981	495,000,000	435,250,000	----------
New Prison Construction Bond Act of 1984	300,000,000	277,500,000	----------
New Prison Construction Bond Act of 1986	500,000,000	----------	500,000,000
Parklands Acquisition and Development Act of 1980	285,000,000	182,175,000	45,000,000
Recreation and Fish and Wildlife Enhancement Act of 1970	60,000,000	21,000,000	----------
Safe Drinking Water Bond Law of 1976	175,000,000	137,370,000	15,000,000
Safe Drinking Water Bond Law of 1984	75,000,000	18,000,000	55,000,000
Safe Drinking Water Bond Law of 1986	100,000,000	----------	100,000,000

Table 1 (continued)

SUMMARY OF AUTHORIZED AND OUTSTANDING STATE GENERAL OBLIGATION BOND PROGRAMS
AS OF JUNE 30, 1987

Bond Authorization	Amount Authorized	Amount Outstanding	Amount Unissued
Senior Center Bond Act of 1984	$50,000,000	$47,500,000	----------
State Beach, Park, Recreational and Historical Facilities	400,000,000	156,860,000	----------
State Construction Program Bonds	1,050,000,000	155,200,000	----------
State Higher Education Construction Program Bond Act of 1966	230,000,000	52,080,000	----------
State School Building Lease-Purchase Bond Law of 1982	500,000,000	414,655,000	----------
State School Building Lease-Purchase Bond Law of 1984	450,000,000	245,000,000	$200,000,000
State School Building Lease-Purchase Bond Law of 1986	800,000,000	----------	800,000,000
State Urban and Coastal Park Bond Act of 1976	280,000,000	160,390,000	25,000,000
Water Conservation and Water Quality Bond Law of 1986	150,000,000	----------	150,000,000
TOTAL GENERAL FUND BONDS	**$9,845,900,000**	**$3,410,560,000**	**$4,135,000,000**
SELF-LIQUIDATING (Enterprise Fund Bonds)			
California Water Resources Development Bond Act of 1959	1,750,000,000	1,364,725,000	180,000,000
Harbor Development Bond Law of 1958	60,000,000	12,650,000	----------
San Francisco Harbor Improvement Act	29,303,000	375,000	----------
State School Building Aid Bonds	2,140,000,000	416,475,000	40,000,000
Veterans Bonds	5,950,000,000	2,823,765,000	850,000,000*
TOTAL ENTERPRISE FUND BONDS	**$9,929,303,000**	**$4,617,990,000**	**$1,070,000,000**
TOTAL STATE GENERAL OBLIGATION BONDS	**$19,775,203,000**	**$8,028,550,000**	**$5,205,000,000**

*This amount was approved on June 3, 1986.

Source: State Treasurer's Office, August 31, 1987

Table 2

SUMMARY OF CONSTITUTIONAL PROVISIONS RELATING TO STATE GENERAL OBLIGATION BONDS

Subject	Section
Authority to issue general obligation bonds; general obligation bond statutes may not be repealed	Article XVI Section 1
Approved purposes are limited to a single subject	Article XVI Section 1
Time limit on maturity is limited to 50 years	Article XVI Section 1
Legislative Process; requires 2/3's approval of both houses; legislation may reduce authorized amount if work is not yet contracted	Article XVI Section 1
Voter Process; requires majority approval at primary or general election	Article XVI Section 1
Financial Provisions Authorizes establishment of proceeds fund; Prohibits bond issues as constitutional amendments.	Article XVI Section 1 Section 2
Taxation; exempts State and local bonds from property taxation; income taxation	Article XIII Section 3(c) Section 26(c)
Appropriations Prohibits impairment of meeting bond obligations; Excludes debt service from appropriations limit	Article XIIIB Section 7 Section 9
Deposit of public money; Provides for payment of debt service by fiscal agents	Article XI Section 11(b)
Initiative process; Authorizes voter initiation of bond measures	Article II Section 8(a)

Table 3

SUMMARY OF STATUTORY PROVISIONS RELATING TO STATE GENERAL OBLIGATION BONDS

Subject	Section*
General provisions	Chapter 1 Section 16650
Designation of State fiscal agent	Chapter 2 Section 16670
Replacement of lost/stolen bonds	Chapter 3 Section 16700
General Obligation bond issuance	Chapter 4
Bond issuance process	Section 16720
Maturity of bonds	Section 16720 (b)
Interest rate limit of 11%	Section 16720 (d)
Interest rate need not be uniform for all bonds of the same issue	Section 16733
Authority for bond anticipation notes	Section 16736
Preparation and execution of bonds	Section 16740
Sale of bonds	Section 16750
Bid deposit requirement of 0.5%	Section 16753
Competitive sale to be based on lowest interest cost	Section 16754
Authority for negotiated sale	Section 16754.3
Bond discount may not exceed 5%	Section 16754.3
Authority to obtain legal opinion	Section 16760
Authority to call and redeem prior to maturity	Section 16774

*All references are to Division 4, Part 3 of the California Government Code.

Legislation authorizing individual general obligation bond programs and specifying the amount of general obligation bonds to be issued must be approved by a two-thirds majority of both houses of the State Legislature and signed into law by the Governor. A ballot measure is then placed before the voters in a general or primary election. The measure must receive a majority of the votes cast.

For the most part, State agencies involved in the implementation of general obligation bond programs either administer the program to expend bond proceeds (i.e., the administering agency), approve the sale of bonds (i.e., the finance committee), or sell and service the bonds (i.e., the State Treasurer's Office).

The legislation authorizing general obligation bonds generally designates a State agency to administer the program and to expend the bond proceeds. For example, the Department of Parks and Recreation reviews and approves applications from local agencies for grants to construct local park facilities under the Community Parklands Bond Act program.

Each bond program also establishes a finance committee to authorize the sale of the general obligation bonds. Members of the finance committee are generally specified in the authorizing legislation, and typically include the State Treasurer, the Director of Finance, and the State Controller. The administering department, such as the Department of Parks and Recreation in the previous example, determines the amount needed, includes the amount in the Budget Act, and then submits the information to the finance committee. The finance committee reviews the proposed amount of the sale and forwards its approval to the State Treasurer for the sale of the bonds.

As a response to the federal Tax Reform Act of 1986 limits on arbitrage, State legislation now authorizes the approval of interim loans from the Pooled Money Investment Account to be made to administering agencies to carry out programs, in anticipation of selling the general obligation bonds. When the State general obligation bonds are sold, the proceeds will be used to reimburse the Pooled Money Investment Account. Until additional State legislation is enacted and further clarification of federal arbitrage rules is obtained, this process is the only mechanism available to raise funds for programs or facilities authorized by State general obligation bond statutes.

D. HISTORY OF STATE GENERAL OBLIGATION BOND BALLOT MEASURES

Since 1900, California voters have considered $24,645,950,000 in 110 ballot measures, and approved 88 ballot measures totalling $20,442,700,000. This represents an 80.0 percent approval of all State general obligation bond measures considered in the 48 elections since 1900.

Table 4 below presents a summary of State general obligation measures considered in each decade since 1900. The results of all State general obligation bond elections held from 1900 through 1986 are summarized in Table A-1 on pages A-1 through A-7.

The margin of approval of bond measures was larger in earlier years of this century. Prior to 1960, 71.0 percent of the approved measures received greater than 65.0 percent of the vote, compared with 38.0 percent receiving more than 65.0 percent in the period after 1960. However, in three consecutive elections five of nine bond measures failed. This period, encompassing the June 1976, November 1976, and June 1978 elections, saw the voters defeat 55.6 percent of the measures placed on the ballot.

Table 4

SUMMARY OF STATE GENERAL OBLIGATION BOND MEASURES CONSIDERED IN EACH DECADE SINCE 1900

	MEASURES CONSIDERED		MEASURES APPROVED	
Dates of Election	Amount	Number	Amount	Number
1980-1986	$9,675,000,000	28	$9,095,000,000	26
1970-1979	5,527,200,000	21	3,705,900,000	14
1960-1969	5,500,000,000	17	4,730,000,000	13
1950-1959	2,290,000,000	12	2,290,000,000	12
1940-1949	380,000,000	3	380,000,000	3
1930-1939	107,950,000	5	94,000,000	4
1920-1929	1,098,500,000	10	85,500,000	6
1910-1919	62,300,000	11	60,300,000	9
1900-1909	5,000,000	3	2,000,000	1
TOTAL	$24,645,950,000	110	$20,442,700,000	88

1. Largest and Smallest Bond Measures

The largest single State general obligation bond issue considered by the voters since 1900 is the $1,750,000,000 California Water Project measure approved in November 1960. The largest number of bond issues on one ballot was six measures--appearing on the November 1984 ballot and the November 1914 ballot. However, the largest volume appearing on one ballot was $1,800,000,000 in four issues, considered on the November 1986 ballot. Table 5 presents the largest number and volume of general obligation bond measures on one ballot.

Table 5

LARGEST NUMBER AND VOLUME OF STATE GENERAL OBLIGATION BOND MEASURES ON ONE BALLOT 1900-1986

LARGEST NUMBER OF ISSUES ON ONE BALLOT

Date of Election	Number of Measures	Amount Considered
November 6, 1984	6	$1,650,000,000
November 3, 1914	6	17,800,000
November 1, 1982	5	1,515,000,000

LARGEST VOLUME ON ONE BALLOT

Date of Election	Number of Measures	Amount Considered
November 4, 1986	4	$1,800,000,000
November 8, 1960	1	1,750,000,000
November 6, 1984	6	1,650,000,000

The smallest single bond issue considered was $750,000 for State fairgrounds construction, which was defeated in 1914. The smallest amount approved, $1,000,000, was for measures appearing on the 1910, 1914, and 1928 ballots. Since World War II, the smallest issue considered was $25,000,000 for residential energy conservation, which was defeated in 1976. The smallest approved issue for the same period was $50,000,000 for senior centers approved in 1984. Tables 6 and 7 on the next page list the ten largest and smallest general obligation bond measures considered by California voters from 1900 to 1986.

Table 6

TEN LARGEST STATE GENERAL OBLIGATION BOND MEASURES
1900-1986

Date of Election	Amount	Purpose	Pass/ Fail
November 8, 1960	$1,750,000,000	State Water Project	P
June 3, 1986	850,000,000	Veterans Housing	P
November 4, 1986	800,000,000	Education	P
June 3, 1980	750,000,000	Veterans Housing	P
November 6, 1984	650,000,000	Veterans Housing	P
November 4, 1986	500,000,000	State Prisons	P
November 2, 1982	500,000,000	Education	P
November 7, 1978	500,000,000	Veterans Housing	P
November 2, 1976	500,000,000	Housing Finance	F
June 8, 1976	500,000,000	Veterans Housing	P

Table 7

TEN SMALLEST STATE GENERAL OBLIGATION BOND MEASURES
1900-1986

Date of Election	Amount	Purpose	Pass/ Fail
(After 1945)			
November 2, 1976	$25,000,000	Energy Conservation	F
November 6, 1984	50,000,000	Senior Centers	P
November 3, 1970	60,000,000	Parks/Natural Resources	P
November 4, 1958	60,000,000	Harbor Development	P
June 4, 1968	65,000,000	Education	P
(Before 1945)			
November 3, 1914	750,000	State Fairgrounds	F
November 6, 1928	1,000,000	Olympics	P
November 3, 1914	1,000,000	State Facility	P
November 8, 1910	1,000,000	Harbor Development	P
November 3, 1908	1,000,000	Harbor Development	F

2. Purposes

The purposes which have been consistently approved by California voters include veterans housing, educational facilities, and local water and wastewater system improvements. These purposes received 32.3 percent, 26.7 percent, and 16.9 percent, respectively of the total dollar volume of approved bond measures. Table 8 on page 16 presents the results of bond elections since 1900 according to the purpose of the bond measure.

Table 8

SUMMARY OF STATE GENERAL OBLIGATION BOND MEASURES CONSIDERED SINCE 1900 BY PURPOSE*

	APPROVED			FAILED			TOTAL CONSIDERED		
Purpose	Amount (000s)	Number	Percent of Total	Amount (000s)	Number	Percent of Total	Amount (000s)	Number	Percent of Total
Corrections	$2,320,000	6	11.35%	---	-	---	$2,320,000	6	9.41%
Education	5,461,200	22	26.71%	$1,546,300	6	36.79%	7,007,500	28	28.43%
Energy/Environmental Waste	100,000	1	0.49%	25,000	1	0.59%	125,000	2	0.51%
Harbor Development	83,500	6	0.41%	3,000	2	0.07%	86,500	8	0.35%
Highways	73,000	3	0.36%	10,000	1	0.24%	83,000	4	0.34%
Housing	200,000	1	0.98%	600,000	2	14.27%	800,000	3	3.25%
Parks/Natural Resources	1,671,000	10	8.17%	730,000	3	17.37%	2,401,000	13	9.74%
State Facility Construction	404,000	4	1.98%	285,950	4	6.80%	689,950	8	2.80%
Veterans Housing	6,585,000	22	32.21%	---	-	---	6,585,000	22	26.72%
Water/Waste Water	3,450,000	9	16.88%	---	-	---	3,450,000	9	14.00%
Miscellaneous									
Land Settlement	---	-	---	3,000	1	0.07%	3,000	1	0.01%
Olympics	1,000	1	0.00%	---	-	---	1,000	1	0.00%
Senior Center	50,000	1	0.24%	---	-	---	50,000	1	0.20%
Unemployment Relief	44,000	2	0.22%	---	-	---	44,000	2	0.18%
Water and Power	---	-	---	1,000,000	2	23.79%	1,000,000	2	4.06%
TOTAL	$20,442,700	88	100.00%	$4,203,250	22	100.00%	$24,645,950	110	100.00%

*Percent of total is calculated on the basis of the dollar amount not the number of measures.

Source: California Debt Advisory Commission, August 31, 1987

E. AUTHORIZED BUT UNISSUED STATE GENERAL OBLIGATION BONDS

As of June 30, 1987, the authorized amount of general obligation debt totalled $19,775,203,000. Of this amount, $5,205,000,000 is yet unissued and $8,028,550,000 is outstanding. The difference between the amount authorized and the sum of outstanding and unissued figures is the amount that has been retired. (Table 1 on pages 8 and 9 depicts all State general obligation bond programs and their respective amounts authorized, outstanding and unissued.)

As of June 30, 1987, there were 18 general obligation bond programs in which more than 40.0 percent of the original amount authorized was unissued. These 18 programs account for 92.0 percent of the total of unissued State general obligation bonds. Of the 18 programs, eight were approved by the voters in 1986. The remaining ten programs account for 27.0 percent of the total unissued State general obligation bonds.

Of this authorized but unissued amount, approximately $631,000,000 in loans from the Pooled Money Investment Account have been made as of July 31, 1987. These loans will be retired through the issuance of State general obligation bonds. Of the approximately $631,000,000 which has been loaned, an estimated $15,000,000 has been spent by the administering agencies as of July 31, 1987.

According to the Trust Services Division of the State Treasurer's Office, there are several factors affecting the timing of issuance of general obligation bonds. These include: 1) for measures approved in 1986, the normal delay associated with developing program parameters as well as new limits of the federal Tax Reform Act of 1986; 2) a change in the conditions which prompted the need for the program; 3) administrative delays; 4) lack of an appropriation, where needed; and 5) difficulty in achieving program requirements, such as local funding match.

F. PENDING STATE GENERAL OBLIGATION BOND MEASURES

Thirty-one bills authorizing State general obligation bond sales totalling $14,495,000,000 are pending in the California Legislature as this report is written. (As was stated earlier, this total includes duplicate amounts for certain programs which are proposed in both Assembly and Senate bills.) These measures could be considered at either the June or November 1988 elections. While most of the bills have passed their house of origin, no consensus appears to have yet developed concerning which measures will be placed on the ballot. This consensus may be expected to develop as the election dates approach.

Table 9 on pages 19 and 20 summarizes the 31 bills currently pending. While a number of these measures propose the continuation of the financing of programs through bonds (e.g., veterans housing, safe drinking water), other measures propose to fund new programs through bond proceeds (e.g., State transportation program, child care facilities).

Additionally, an initiative authorizing a State general obligation bond issue of $776,000,000 to provide funds for parks, wildlife, coastal, and natural lands is being circulated. As an initiative, this measure completely obviates the need for legislative and gubernatorial approvals.

IV. STATE POLICY CONSIDERATIONS CONCERNING THE USE OF STATE GENERAL OBLIGATION BONDS

Generally, policy making with regard to the use of State general obligation bonds has developed as a response to specific pieces of legislation which propose to authorize various bond programs. Individual programs are proposed, considered, possibly enacted, and then approved or rejected by the State's voters. This section highlights the participation of the State Treasurer, the Governor's Administration, and the California Legislature in the development of policy concerning the use of State general obligation bonds.

A. THE STATE TREASURER'S OFFICE

The State Treasurer's Office, as the agent for sale of all State debt offerings and the trustee for all State general obligation bonds, closely monitors the proposed use of general obligation bonds by the State of California. Those factors most closely watched include:

- Financial Integrity--Is the proposed financing sound? Is it technically well-conceived? If the bond measure is to be self-liquidating, is it structured in such a way to achieve that end?

- Administrative Clarity--Is the agency or department which will spend the proceeds clearly identified? How will bond sales be approved (i.e., through a finance committee)? Does the proposed legislation build on the State's general obligation law contained in Section 16650 of the Government Code

Table 9

SUMMARY OF PENDING STATE GENERAL OBLIGATION BOND BILLS*
AS OF AUGUST 31, 1987

Bill #	Author	Purpose	Amount	Status
AB 48	O'Connell	Schools Facilities	$800,000,000	Senate Appropriations
AB 69	Clute	Veterans Housing	510,000,000	Senate Third Reading
AB 185	Farr	Superconducting Super Collider	560,000,000	Conference
AB 200	Clute	Veterans Home of California	200,000,000	Senate Governmental Organization
AB 639	Killea	Coastal Resources Conservation	200,000,000	Senate Appropriations
AB 671	Katz	Transportation	1,500,000,000	Senate Transportation
AB 755	Eaves	Automated Highways	50,000,000	Assembly Transportation
AB 930	W. Brown	Wastewater - Border	150,000,000	Senate Appropriations
AB 1215	Bronzan	Public Health Facilities	750,000,000	Interim Study
AB 1439	O'Connell	Safe Drinking Water	200,000,000	Senate Appropriations
AB 1467	Moore	Public Broadcasting	75,000,000	Assembly Utilities
AB 1715	Costa	Water Conservation	750,000,000	Senate Appropriations
AB 1720	Costa	Water Quality	600,000,000	Senate Appropriations
AB 1794	Costa	Park, Recreational and Historical Facilities	475,000,000	Assembly Third Reading
AB 1970	Jones	Park and Recreational Facilities	350,000,000	Assembly Water
AB 2315	N. Waters	Water Conservation	400,000,000	Senate Agriculture
AB 2654	Roos	Child Care Facilities	100,000,000	Inactive File

Table 9 (continued)

SUMMARY OF PENDING STATE GENERAL OBLIGATION BOND BILLS*
AS OF AUGUST 31, 1987

Bill #	Author	Purpose	Amount	Status
SB 4	Presley	Wildlife and Natural Areas	$85,000,000	Assembly Ways and Means
SB 22	Bergeson	Schools Facilities	800,000,000	Assembly Ways and Means
SB 81	Garamendi	Superconducting Super Collider	560,000,000	Conference
SB 88	Torres	Earthquake Safety	350,000,000	Assembly Ways and Means
SB 176	Deddeh	Transportation	1,000,000,000	Assembly Transportation
SB 181	Keene	Library Construction	250,000,000	Assembly Ways and Means
SB 278	Watson	Child Care Facilities	100,000,000	Assembly Human Services
SB 468	Presley	New Prison	850,000,000	Assembly Ways and Means
SB 703	Hart	Higher Education Facilities	600,000,000	Assembly Ways and Means
SB 997	Mello	Clean Water	480,000,000	Assembly Desk
SB 1265	Presley	Law Enforcement Training Facilities	250,000,000	Assembly Desk
SB 1487	Bergeson	Water Pollution Control	400,000,000	Senate Agriculture
SB 1664	Presley	Juvenile Facilities	250,000,000	Assembly Ways and Means
SB 1693	Roberti	Housing	850,000,000	Senate Appropriations
		TOTAL:	$14,495,000,000	

*All measures introduced this legislative session have been included in this table regardless of their current status.

Source: State Treasurer's Office, August 31, 1987

- Legal Considerations--Are the goals of the legislation likely to be achieved given existing tax law, especially at the federal level?

- Debt Capacity--What effect would the proposed general obligation program have on the indicators of debt burden which are assessed by the credit rating agencies? What is the cumulative effect of various programs?

- Limits Per Election--Will the total amount of general obligation debt proposed to the voters be excessive? Annual limits of $2,000,000,000 to $2,500,000,000 (an aggregate total for both the primary and general elections) have been agreed upon by State policy makers in the past.

  Presumably, the State's voters may be more likely to reject certain measures if they perceive that general obligation bond financing is being overused. This "overuse" may relate to the number of measures on the ballot, or, perhaps more likely, the aggregate dollar amounts proposed.

The State Treasurer's Office also follows the deliberations on many other measures, such as the State's budget, which directly or indirectly affect California's fiscal health and hence may influence the State's long-term credit ratings.

Lastly, as agent for sale for all State general obligation bonds, the State Treasurer is the conduit to the market and decides how much debt is marketable.

B. THE GOVERNOR'S ADMINISTRATION

As the State's chief executive, the Governor proposes and signs the State budget. Additionally, legislation which proposes to place a State general obligation bond measure on the ballot must be signed by the Governor.

The process for evaluation of general obligation bond measures within the Governor's Administration generally begins with an analysis by a particular department or agency affected by the proposed bond program. That analysis is reviewed by a cabinet-level agency as well as the Department of Finance for program and fiscal impacts. The recommended positions are then forwarded to the Governor's Office for approval.

During his tenure, the Governor has expressed concern about growing levels of State general obligation bonded indebtedness. In 1984, two State general obligation bond bills were vetoed. In the veto messages for these bills, the Governor indicated concern regarding:

- Excessive Amounts Per Election--The Governor expressed concern about placing too much ($2,000,000,000) in State general obligation measures on a single ballot since it "could overload the public's willingness to approve these issues."

- Excessive Amounts of Indebtedness--Similarly, the Governor noted that the State should not increase its general obligation debt burden beyond a prudent level.

The Administration more formally articulated its evolving policy on State general obligation bonds in the 1986-87 Governor's Budget. This statement recognized the use of general obligation bonds as an "important tool for financing some types of expenditures," but warned that "it must not be over used." The budget also restated the concerns expressed in the 1984 veto messages.

The Administration recommended the following guidelines concerning the use of State general obligation bonds in the 1986-87 Governor's Budget:

- Public Benefit for All--The Governor's budget suggested that general obligation bonds should be used for projects which benefit the general population and provide protection, service or use by the general public. This would exclude bonds to assist individuals or bonds for ongoing operations or support activities.

- Borrow Now Rather Than Pay-As-You-Go--The Governor's budget also suggested that general obligation borrowing should be used only when it could be demonstrated that such "borrowing against the future" benefits the general public. Presumably, this demonstration would compare borrowing through State general obligation bonds to financing the project directly on a pay-as-you-go method.

The Administration also suggested the following three concepts which could be useful in developing more specific guidelines on placing general obligation bond authorization before the voters. (It should be noted that more specific guidelines have not been developed and some policy makers have expressed concern about the use and implementation of these concepts.)

- Limit on Debt Service--Consider limiting debt service on general obligation bonds, not including self-liquidating bonds, to not more than five percent of General Fund revenue. (Currently, the State devotes approximately 1.5 percent of all General Fund expenditures to debt service on non self-liquidating general obligation bonds.)

- Limit on Unissued Authorizations--Propose limiting the increase or the percentage increase in unissued general obligation bond authorizations over any two-year period to the increase in General Fund revenue, since these authorizations represent contingent obligations.

- Specify Appropriate Uses--Consider restricting State general obligation measures to "an approved list of uses which could be amended only through a two-thirds vote of the Legislature." This limit on uses would not apply to self-liquidating State general obligation bonds.

  The Governor's budget suggested nine "acceptable" uses for bond financing: school construction, clean water, water conservation, safe drinking water, toxic cleanup and waste management, local jails, State prisons, fish and wildlife habitation enhancement, and state beach, park, recreational and historical facilities.

C. THE CALIFORNIA LEGISLATURE

The California Legislature's role in the approval of State general obligation bonds emanates from Section XVI of the California Constitution. Section XVI requires that legislation proposing general obligation indebtedness be approved by two-thirds of the members of the Assembly and the Senate before it may be considered by the voters.

In the Senate, general obligation bond measures are heard by the policy committee having purview over the program proposed by the measure as well as by the Senate Appropriations Committee.

The process is similar in the Assembly except that all bond measures are considered by the Public Employees and Bonded Indebtedness Subcommittee of the Assembly Ways and Means Committee. Bills are heard by this subcommittee after consideration by the appropriate policy committee, but before consideration by the full Assembly Ways and Means Committee.

Written policy guidelines were adopted by the now-disbanded Assembly Public Investments, Finance, and Bonded Indebtedness Committee in January 1986 for use in its review of State general obligation bond bills proposed for 1986 ballots. These guidelines were as follows:

- Public Benefit--Non self-liquidating bond programs should benefit the general population of the State. Proceeds should not be used for grants to private parties.

- Capital Outlay--Bonds should be used solely for capital construction, remodeling, renovation, or rehabilitation of facilities and related land acquisition. Proceeds should not be used for working capital, consumables, or for support activities.

- Federal Tax Reform--The proposed bond measure was to be examined in light of the then-proposed federal tax law changes. The Committee guidelines suggested that measures that would not qualify as tax-exempt or measures which would exhaust significant portions of the State's volume cap should not be placed on the ballot.

In addition, the Legislative Analyst Office analyzes proposed State general obligation bonds as they are considered by the California Legislature.

Finally, the current legislative session's Assembly Constitution Amendment 16 (McClintock) proposes to amend Section XVI of the California Constitution by specifying that State general obligation bonds may only be used for "capital improvements which serve a public purpose and which are undertaken by any state agency." This constitutional amendment has been assigned to the Assembly Ways and Means Committee.

D. JOINT DECISION-MAKING BY STATE POLICY MAKERS

It is within the legislative context where many of the difficult decisions about which State general obligation bond measures should be placed on the ballot have been made in the past few years. Bills proposing State general obligation bond financing have often totalled more than most policy makers believe should be placed on the ballot. For example, in the 1985-86 legislative session, more than $7,200,000,000 in State general obligation measures were proposed at one time.

As such, the State Treasurer, the Administration, and leaders of the majority and minority parties in both the Senate and the Assembly have come together to explore and to determine the total dollar amount of State general obligation bond authorizations to be placed on the ballot, as well as which measures seem to have the highest priority. Together, these policy makers agreed that $1,600,000,000 and $1,800,000,000 in State general obligation measures should be placed on the June 1986 and November 1986 ballots, respectively, from the 1985-86 legislative session.

Often, decisions such as the ones arrived at in 1986 are finalized just before the Secretary of State's deadline for preparation and printing of the voters' pamphlets and ballots.

As this report indicates, this informal process has worked reasonably well. Target maximum amounts of general obligation bond authorization to be placed on the ballot have been set. Programs which serve the general public have, for the most part, received a priority over those which do not.

However, the ad hoc nature of this process underscores the need for policy makers to pay extremely close attention to assuring that discretion is exercised regarding the use of the State's general obligation debt capacity. In this context, State policy makers must balance: 1) the safe-guarding of the State's credit rating; 2) a commitment to making adequate and timely investments in needed State programs, facilities, and infrastructure; and 3) protecting future Californians from excessive bonded indebtedness.

V. CREDIT RATING AGENCIES' PERSPECTIVES

Standard & Poor's Corporation, Moody's Investors Service, Inc., and Fitch Investors Service, Inc. are the three major municipal credit rating agencies. Each evaluates the creditworthiness of State and local debt issues at the request of the issuers (or authorized representatives on their behalf).

All assign letter ratings to indicate the relative quality of municipal credits. Although the symbols used vary slightly, the rating which indicates the highest quality is AAA (or Aaa). Three additional ratings are also considered investment quality: AA (Aa), A, and BBB (Baa). According to the rating agencies, any issue rated less than BBB (Baa) is of speculative investment grade. Table 10 below summarizes the ratings used by all three agencies.

Table 10

SUMMARY OF LONG-TERM MUNICIPAL CREDIT RATINGS

	S&P	Moody's	Fitch
INVESTMENT GRADE			
Best/highest quality	AAA	Aaa	AAA
High quality	AA	Aa	AA
Good/upper medium quality	A	A	A
Medium quality	BBB	Baa	BBB
SPECULATIVE GRADE	BB, B, CCC CC	Ba, B, Caa Ca, C	BB, B, CCC CC, C

The current state general obligation ratings assigned by all three rating agencies are summarized in Table 11 on page 27 and 28.

The rating process used and rating factors considered by all three municipal credit rating agencies are described in detail in publications provided by each agency. While the processes used and factors considered by the three agencies in their analyses are similar, industry observers note that credit analysis "remains more an art than a science," requiring "individual judgment and personal interpretation of a range of important factors."

Notwithstanding this observation, the rating agencies examine four principal factors in their credit analysis--the economy, financial indicators, debt factors, and administrative and governmental factors.

Table 11

SUMMARY OF STATE GENERAL OBLIGATION BOND RATINGS

	S&P	Moody's	Fitch
ALABAMA	AA	Aa	--
ALASKA	AA-	Aa	--
ARIZONA	--	--	--
ARKANSAS	AA	A1	--
CALIFORNIA	AAA	Aa	AAA
COLORADO	--	--	--
CONNECTICUT	AA+	Aa1	--
DELAWARE	AA	Aa	--
FLORIDA	AA	Aa	AA
GEORGIA	AA+	Aaa	AAA
HAWAII	AA	Aa	--
IDAHO	--	--	--
ILLINOIS	AA+	Aaa	AAA
INDIANA	--	--	--
IOWA	--	--	--
KANSAS	--	--	--
KENTUCKY	AA	Aa	--
LOUISIANA	A-	A	--
MAINE	AAA	Aa1	--
MARYLAND	AAA	Aaa	--
MASSACHUSETTS	AA	A1	AA
MICHIGAN	AA-	A1	--
MINNESOTA	AA+	Aa	--
MISSISSIPPI	AA-	Aa	--
MISSOURI	AAA	Aaa	--
MONTANA	AA-	Aa	--
NEBRASKA	--	--	--
NEVADA	AA	Aa	--
NEW HAMPSHIRE	AA+	Aa	--
NEW JERSEY	AAA	Aaa	AAA
NEW MEXICO	AA	Aa	--
NEW YORK	A+	A1	A

Table 11 (continued)

SUMMARY OF STATE GENERAL OBLIGATION BOND RATINGS

	S&P	Moody's	Fitch
NORTH CAROLINA	AAA	Aaa	AAA
NORTH DAKOTA	AA-	Aa	--
OHIO	AA	Aa	--
OKLAHOMA	--	Aaa	--
OREGON	A+	A1	A+
PENNSYLVANIA	AA-	A1	A+
RHODE ISLAND	AA	Aa	AA
SOUTH CAROLINA	AAA	Aaa	AAA
SOUTH DAKOTA	--	--	--
TENNESSEE	AA+	Aaa	AAA
TEXAS	AA+	Aaa	--
UTAH	AAA	Aaa	--
VERMONT	AA	Aa	AA
VIRGINIA	AAA	Aaa	--
WASHINGTON	AA	A1	--
WEST VIRGINIA	AA-	A1	--
WISCONSIN	AA	Aa	AA
WYOMING	--	--	--
TOTAL STATES RATED	40	41	15

SOURCE: Standard & Poor's Corporation, Moody's Investors Service, Inc. and Fitch Investors Service, Inc.

The remainder of this section summarizes the approach of the three major credit rating agencies in analyzing state general obligation debt. This detail was provided by representatives of each of the three rating agencies.

A. STANDARD & POOR'S CORPORATION

Standard & Poor's has rated municipal issues since 1940. Forty states currently have general obligation bond ratings from Standard and Poor's. California, and eight other states, have the highest possible long-term credit rating from Standard & Poor's--that of AAA.

1. Rating Factors for State General Obligation Debt

Standard & Poor's considers the economic base of the state the most critical element in determining a general obligation issuer's rating. Standard & Poor's looks for strength and diversity in a state's economy, reflecting Standard & Poor's philosophy that a strong, recession-hardy economy will generate revenues needed to repay debt. In assessing a state's economic base, Standard & Poor's examines:

- Issuer Characteristics--This involves taking a macro-economic view of the issuer: its location, transportation network, infrastructure, natural assets, and liabilities.

- Demographics--This trend analysis spans over a forty-year period. Here, population growth trends, age group composition, and income data (e.g. personal income, per capita retail sales, and transfer payments) are evaluated.

- Tax Base--The focus in this factor is on economic diversity and growth. Building activity and tax revenue generation by industry group are among the elements examined. Additionally, Standard & Poor's assesses the extent to which a state's tax base may be affected by the growth or lack of growth in regional economies.

- Employment Base--This factor includes labor force trends, unemployment levels, and employment by industry group.

Financial indicators also contribute to Standard & Poor's rating by depicting the extent to which a state's financial flexibility may be constrained. Among the most important financial elements are:

- <u>Accounting and Financial Reporting Methods</u>--This analysis evaluates a state's treatment of revenues and expenditures as well as assets and liabilities based on the guidelines of generally accepted accounting principles. Audits by independent certified public accountants are expected to be provided.

- <u>Budget</u>--Standard & Poor's closely examines a state's budget looking at both expenditures and revenues and any significant changes in budget categories. The source of the revenues and a state's relative tax burden is also assessed. In terms of rainy-day reserves, Standard & Poor's generally recommends a target of five percent of the budget for states. It is further recommended that debt service costs as a percentage of total expenditures be moderate--not more than five percent of total expenditures.

- <u>Off-Balance Sheet Liabilities</u>--Pension liabilities and other "hidden" obligations are identified. Standard & Poor's likes to see a state acknowledge its obligations and plan to take steps to minimize unfunded obligations.

Debt factors are the third major area assessed by Standard & Poor's. Standard & Poor's first assesses the type of general obligation pledge underlying the issue. It then evaluates:

- <u>Maturity Schedule</u>--Prudent use of debt dictates that the bond's term matches the useful life of the facilities being financed. An average maturity schedule for capital projects is one in which 25 percent of the debt is retired in five years, and 50 percent is retired in ten years. A faster maturity schedule may be viewed negatively, if it puts excessive strain on the operating budget.

- <u>Debt Limitations and Needs</u>--Unrealistic debt limits are not viewed positively by Standard & Poor's. Restrictive debt limits may result in the creation of financing mechanisms that do not require general obligation bond authorization or voter approval. These limits may also restrict an issuer's ability to borrow in the event of an emergency. To assess the debt burden on a state's taxpayers, Standard & Poor's prepares a debt statement. This statement identifies gross and direct net debt issued by the state as well as overall net debt.

  <u>Gross debt</u> for California includes not only the State's general obligation bonds, but also includes any obligation secured either directly or indirectly by State general fund revenues (e.g., public lease revenue bonds for State prisons). Additionally, debt not issued by the State, but secured by the State would be included in gross debt. <u>Direct net debt</u> for California is the State's gross debt as defined above less any "sinking fund" or "self-liquidating" debt such as veterans bonds.

  <u>Overall net debt</u> represents not only state direct net debt but also debt issued by local agencies secured by general tax revenues--regardless of whether these taxes are state or local in nature. According to Standard & Poor's, this measure provides comparability among states to balance the differences in how responsibilities are shared between local and state governments.

  Using this overall net debt figure, Standard & Poor's calculates the Standard & Poor's Index which indicates an "ability to pay." California's current Standard & Poor's Index is 6.3. A state Standard & Poor's Index less than five is considered low, while one above 12 or 13 is very high. In general, low debt is not necessarily good because it may indicate that the state is not making adequate investments to maintain its economic base. Standard & Poor's also examines future financing needs, looking for regular capital needs assessments and planning for capital improvements.

Lastly, Standard & Poor's considers administrative factors in determining a general obligation rating.

- Tax Structure--Does the state benefit from the economic activity within its boundaries? How flexible, both legally and politically, is the taxing structure?

- Pending Litigation--How could pending litigation affect the issuer?

- Financial Management--How are financial decisions made? Where does the power reside? Who makes projections of revenues and expenditures? Are projections realistic and are they achieved? Is the budget adopted on time? Is there a central point for issuing and tracking debt?

- Labor Relations--What is the relationship between the state as employer and its employees? Are negotiations resolved on a timely basis?

2. Comments on California

In upgrading California's rating to AAA last summer, Standard & Poor's acknowledged a strong outlook for economic growth and vitality, sound financial management, commitments to addressing pension liabilities, and a solid financial position with good prospects for maintaining prudent reserves.

Standard & Poor's noted that the State is committed to funding an adequate reserve. Additionally, the rating agency recognized that the Gann limit "may put pressure on pension funding in the future, and help prevent a repeat of the explosive spending growth experienced during 1978-83."

B. MOODY'S INVESTORS SERVICE, INC.

Moody's has rated tax-exempt municipal debt since 1918. Over 26,000 ratings on the long- and short-term debt of 18,000 state and local agencies are currently outstanding. Twelve states are currently rated Aaa by Moody's. California is currently rated Aa.

1. <u>Rating Factors for State General Obligation Debt</u>

Unlike Standard & Poor's and Fitch, Moody's does not consider the economy to be the dominant factor in the analysis of a municipal credit. Rather, Moody's emphasizes the interrelationships among the four rating factors--debt, administrative and governmental, economic, and financial factors. As a Moody's representative indicated, when Moody's assigns a rating to a debt issue, it is rating the debt, <u>not</u> the economy.

Moody's publishes debt indicators which are updated annually from its files and municipal data base. These medians are used as a guide to the Moody's analyst in assessing the debt of the issuer as a rating analysis is being prepared. For state level debt, Moody's prepares three different debt indicators:

- net tax-supported debt per capita;
- net tax-supported debt as a percent of estimated full valuation; and
- net tax-supported debt as a percent of personal income.

Tax-supported debt, as perceived by Moody's, includes all debt serviced by the tax revenues of the state, regardless of whether the state itself was the issuer. Net tax-supported debt excludes any debt which is self-supporting from enterprise revenues, debt which is serviced by another government unit, as well as sinking-fund debt and short-term operating debt.

Although these medians are not absolute indicators of credit quality, they do provide broad guidelines to the Moody's analyst. Moody's particularly looks at trends in movement of the debt indicators in relation to the median as well as divergence from the median as indications the state may becoming too indebted. Critical to the debt analysis is a close examination of the pledged legal security and other bond holder protections.

Moody's also looks for whether the debt structure limits future flexibility and the extent to which debt is payable from earmarked revenues. If a large percentage of revenue is earmarked for debt service, Moody's may perceive a potential problem in the ability of a state to provide basic services during economic downturns.

In terms of debt, Moody's indicates that it does not closely examine the purpose of the general obligation debt financings as long as the full faith, credit, and taxing power pledge is made. However, Moody's did note that it believes the "safest" general obligation debt to be issued is for clearly-identifiable general governmental purposes. According to Moody's, narrow special purpose general obligation debt often is unwise and may represent a large future drain on revenues. As such, defaults on these bonds may be more likely to occur.

Moody's also does not view positively strict self-imposed limits on the use of debt. Moody's notes that these limits are generally either so restrictive that they lead to circumvention of the limit through some new financing mechanism or are so lax that they are meaningless. Moreover, Moody's indicated that such limits can severely encumber a state's ability to respond swiftly and with certainty to a pressing policy issue.

Financial factors are also considered by Moody's in its analysis of state general obligation issues. Among the issues reviewed:

- Budget--Is the budget balanced and does it include a reserve? (Moody's recommends a minimum reserve of five percent of revenues.)

- Revenue and Expenditures--What are the sources of the revenue? Are the sources diversified and stable? (Moody's notes that sales taxes and income taxes are increasingly responsible for revenue generation.) What makes up the expenditures?

- Financial History--Is there a record of sound financial operations? A history of swift action in tough times?

- Short-term Debt--Does the short-term debt come due on the same date and in large amounts?

- Debt Burden--Does debt service compete with expenditures for current operations? (Moody's notes that debt service should not generally exceed eight percent of revenues.) The choice should not be between employees and bondholders.

In terms of administrative and governmental factors, Moody's examines:

- Type of Governmental Organization--Strong executives are generally viewed positively while boards and commissions with diffused accountability are not looked upon as favorably.

- Budget Process--Does the legislature thoughtfully and responsibly consider the budget? Is there an independent, nonpartisan legislative analyst? Are costs clearly identified in bills?

- Financial Reporting--Type, timing, and frequency of financial reporting.

- Revenue Forecasting--Type, timing, and frequency of revenue forecasting.

- Unfunded Pension Liabilities--Presence and extent of unfunded pension liabilities.

- Intergovernmental financial relationships.

- Initiatives--Are initiatives used as a forum for complex financial lawmaking?

In terms of the economy, Moody's notes that it is difficult to isolate any one measure that is most important in its analysis. On the whole, Moody's looks for wealth and stability which implies diversity, and adaptability. However, Moody's terms the economy the "least controllable and often the most difficult factor to predict in municipal credit analysis."

Some of the economic measures evaluated include employment by industry group, unemployment, sources of and trends in personal income, population trends, and social characteristics. Through trend analysis, Moody's attempts to focus not only on the current condition of the state's economy, but where it may be headed.

Investments in infrastructure to develop and maintain an economy are also very important in the Moody's analysis. However, here Moody's notes that it is often difficult to obtain accurate needs assessments which are not "wish lists." Moody's indicates that personal observations and discussions with state and local representatives are often more valuable than depending on formal needs assessments.

2. Comments on California

In its analysis of the State's last general obligation bond sale in July 1986, Moody's noted that California has low debt ratios due to the self-supporting nature of a large portion of general obligation bonds. Financial operations, in Moody's opinion, have stabilized and a comfortable budget surplus has accumulated. However, Moody's notes that unexpected natural disaster relief costs could reduce the reserve. Finally, California's wealth and developments are acknowledged, although Moody's states that "frequent initiative actions and assumption by [the] state of local functions still pose uncertainties to the bond holder."

C. FITCH INVESTORS SERVICE, INC.

Fitch Investors Service has been actively rating municipal bonds since 1980. Fifteen states' general obligation bonds currently are rated by Fitch. California is rated AAA by Fitch, as are six other states.

1. Rating Factors for State General Obligation Debt

As does Standard & Poor's, Fitch considers the economy the single most important element in a state general obligation bond rating. Simply stated, the economy drives the process by generating revenues to repay debt.

Debt policy is increasingly important to the rating, according to a Fitch representative. Fitch evaluates whether there is a consensus which supports the debt. Debt in relation to personal income, rather than per capita debt, is emphasized. Fitch also assesses whether there is a pattern to debt issuance and whether debt issuance is reasonably related to debt retirement in such a way that future flexibility is afforded. In this context, Fitch also looks at total outstanding indebtedness as compared to total authorized debt.

Financial factors are also important. Fitch analyzes the state's expenditure policy and its spending priorities as well as its budget reserve. A balanced budget is a must. A broad tax base is a plus. In contrast, long-term debt financing of current operations is seen as a symptom of fiscal weakness.

Lastly, administrative and management factors are considered by Fitch--with these factors being the most intangible and qualitative of the four.

2. Comments on California

In July 1986, Fitch Investors Service raised California's general obligation rating from AA+ to AAA. The upgrade was attributed to three straight years of "strengthened finances" and low debt in relation to personal income as well as continued low debt per capita. The rating agency cited the strong and highly diversifed economy and the related increases in personal income and employment, which account for the strong revenue base in retail sales and use taxes and personal income taxes. Fitch also noted that the State's constitutional expenditure limit would in fact limit expenditures despite continuing anticipated revenue growth.

VI. CALIFORNIA COMPARED TO OTHER STATES

This section draws a number of comparisons between California and the other states in the nation. First, debt capacity and debt burden as measured by certain debt indicators is examined. Second, each state's constitutional and/or statutory authority regarding general obligation bond debt is outlined. Third, debt management policies of selected states concerning the use of general obligation debt are presented. Fourth, the use of general obligation bond proceeds by 40 of the 50 states is summarized.

A. DEBT CAPACITY AND DEBT BURDEN

According to all commonly accepted indicators, the State of California is well within reasonable benchmarks for general obligation debt burden. Debt capacity and debt burden indicators are useful as standard tools for comparing California to the rest of the nation because the data is readily available which facilitates comparison among the states. However, it may not always be appropriate to make standard comparisons which do not take into consideration the importance of personal income as a driving force of revenue and, therefore, debt capacity. In addition, standard indicators alone do not incorporate any information about capital improvement needs or a state's management or administrative structure.

With these limitations in mind, one can use debt indicators as an initial starting point in an evaluation of a state's general obligation debt.

A primary method of measuring debt affordability is to calculate the ratio of annual debt service to current expenditures. This ratio is a gauge of the impact, or strain, of debt repayments on a state budget. Table 12 on page 38 summarizes debt service as a percentage of total budget expenditures for selected states. Of those states rated AAA by Standard & Poor's, California ranked in the lower third when comparing the percentage of state expenditures targeted to debt service. For the 1986-87 fiscal year, $530,021,000 in principal and interest payments from the general fund will support non self-liquidating general obligation debt.

Table 12

DEBT SERVICE AS A PERCENTAGE OF STATE EXPENDITURES FOR SELECTED STANDARD & POOR'S RATED STATES AS OF JULY 31, 1987

AAA States	% of State Expenditures
MARYLAND	9.6
UTAH	8.0
SOUTH CAROLINA	4.3
MAINE	4.2
NEW JERSEY	3.1
NORTH CAROLINA	2.3
CALIFORNIA	1.5
MISSOURI	1.1
VIRGINIA	1.0
AA States	
OHIO	9.1
MASSACHUSETTS	6.3
FLORIDA	5.9
GEORGIA	3.5
ILLINOIS	3.1
TEXAS	1.4
A States	
NEW YORK	4.2

Table 13 on pages 39 and 40 depicts California's position in relation to the other 49 states when comparing debt burden as measured by commonly-used indicators such as debt per capita, debt per $1,000 of personal income and debt as a percentage of estimated full valuation. As reflected in these tables, California currently ranks 32nd in net tax-supported debt per capita, 36th in net tax-supported debt as a percentage of personal income, and 35th in net tax-supported debt as a percentage of estimated full valuation. This may be contrasted with indicators of debt capacity where California ranks fifth in per capita personal income and eleventh in estimated valuation per capita.

Table 13

MOODY'S STATE DEBT MEDIANS

State	Personal Income Per Capita	Rank	Debt Per Capita	Rank	Debt as % of Personal Income	Rank	Debt as % of Full Value	Rank
Aaa								
GEORGIA	$12,543	31	$270	27	2.3	26	1.0	28
ILLINOIS	14,738	10	393	19	2.7	23	1.9	12
MARYLAND	15,864	7	614	9	4.0	12	2.1	10
MISSOURI	13,244	24	146	34	1.1	33	0.6	31
NEW JERSEY	17,211	3	438	15	2.6	24	1.4	24
NORTH CAROLINA	11,617	37	120	37	1.0	37	0.5	37
OKLAHOMA	12,232	33	37	43	0.6	43	0.1	43
SOUTH CAROLINA	10,586	46	186	30	1.8	29	0.9	29
TENNESSEE	11,243	39	119	38	1.1	34	0.6	34
TEXAS	13,483	21	97	41	0.7	41	0.3	41
VIRGINIA	14,542	11	109	40	0.8	40	0.4	38
Aa								
ALABAMA	10,673	45	458	12	4.3	8	2.3	8
ALASKA	18,187	1	1,536	2	8.7	2	2.1	9
CALIFORNIA	16,065	5	165	32	1.0	36	0.5	35
CONNECTICUT (Aa1)	18,089	2	747	5	4.1	11	2.8	6
DELAWARE	14,272	13	1,084	3	7.7	3	3.8	3
FLORIDA	13,742	19	408	16	3.1	16	1.6	18
HAWAII	13,814	17	1,714	1	12.5	1	4.7	1
KENTUCKY	10,824	44	520	10	4.8	7	1.6	19
MAINE (Aa1)	11,887	36	284	26	2.4	25	1.1	26
MINNESOTA	14,087	14	302	25	2.2	27	1.0	27
MISSISSIPPI	9,187	50	146	33	1.7	30	1.2	25
MONTANA	10,974	42	310	24	2.9	19	1.5	22
NEVADA	14,488	12	196	29	1.4	32	0.5	36
NEW HAMPSHIRE	14,964	8	399	18	2.7	21	1.5	21

Table 13 (continued)

MOODY'S STATE DEBT MEDIANS

State	Personal Income Per Capita	Rank	Debt Per Capita	Rank	Debt as % of Personal Income	Rank	Debt as % of Full Value	Rank
Aa (continued)								
NEW MEXICO	$10,914	43	$381	20	3.6	14	1.9	14
NORTH DAKOTA	12,052	35	128	36	1.1	35	0.3	40
OHIO	13,226	25	370	21	3.0	18	1.5	20
RHODE ISLAND	13,906	15	446	13	3.2	15	1.9	13
VERMONT	12,117	34	478	11	4.0	13	1.6	17
WISCONSIN	13,154	27	354	22	2.7	22	1.4	23
A								
ARKANSAS (A1)	10,476	48	31	44	0.3	44	0.2	42
LOUISIANA	11,274	38	719	6	6.4	4	2.7	7
MASSACHUSETTS (A1)	16,380	4	878	4	5.4	5	3.4	4
MICHIGAN (A1)	13,608	20	135	35	1.0	38	0.6	33
NEW YORK (A1)	16,050	6	669	8	4.2	10	4.5	2
OREGON (A1)	12,622	29	186	31	1.6	31	0.6	32
PENNSYLVANIA (A1)	13,437	22	407	17	3.1	17	3.1	5
WASHINGTON (A1)	13,876	16	676	7	4.9	6	1.8	15
WEST VIRGINIA (A1)	10,193	49	442	14	4.3	9	1.9	11
Not Rated								
ARIZONA	12,795	28	110	39	0.9	39	0.4	39
COLORADO	14,812	9	24	45	0.2	46	0.1	44
IDAHO	11,120	41	22	46	0.2	45	0.1	46
INDIANA	12,446	32	7	49	0.06	49	0.05	48
IOWA	12,594	30	0.6	50	0.005	50	0.002	50
KANSAS	13,775	18	78	42	0.6	42	0.1	45
NEBRASKA	13,281	23	15	48	0.1	48	0.1	47
SOUTH DAKOTA	11,161	40	311	23	2.8	20	1.7	16
WYOMING	13,223	26	19	47	0.03	47	0.03	49
Median	$13,867	--	$293	--	2.4	--	1.2	--

Source: Moody's Investors Service, Inc., 1987 Medians, 1987

According to U.S. Census Bureau data, California also compares favorably to national averages when evaluating the trend of growth in personal income per capita and general obligation debt as a percentage of personal income, as depicted in Tables 14 and 15 below.

Table 14

COMPARISON OF TOTAL OUTSTANDING STATE GENERAL OBLIGATION DEBT AS A PERCENTAGE OF PERSONAL INCOME CALIFORNIA AND THE U.S. 1980-1985

	California	U.S.
1980-1981	2.38%	2.43%
1981-1982	1.43%	2.14%
1982-1983	1.38%	2.14%
1983-1984	1.30%	2.10%
1984-1985	1.29%	2.00%

Source: U.S. Department of Commerce, Bureau of the Census, Government Finances.

Table 15

COMPARISON OF PERSONAL INCOME PER CAPITA CALIFORNIA AND THE U.S. 1980-1985

	California	U.S.
1980-1981	$10,938	$9,521
1981-1982	11,923	10,619
1982-1983	12,567	11,107
1983-1984	13,257	11,658
1984-1985	14,487	12,778

Source: U.S. Department of Commerce, Bureau of the Census, Government Finances.

Additionally, as can be seen from the Table 16 below the State's personal income has been increasing at a faster rate than the growth in the State's general obligation debt.

Table 16

COMPARISON OF ANNUAL CHANGES IN PERSONAL INCOME AND FULL FAITH AND CREDIT DEBT CALIFORNIA AND THE U.S. 1980-1985

PERSONAL INCOME

	California		U.S.	
	Amount	% Change	Amount	% Change
1980-81	$259,551,000,000	---	$2,162,936,000,000	---
1981-82	288,481,000,000	+11.1	2,405,600,000,000	+11.2
1982-83	310,704,000,000	+7.7	2,571,592,000,000	+6.9
1983-84	333,741,000,000	+7.4	2,734,122,000,000	+6.3
1984-85	371,202,000,000	+11.2	3,009,601,000,000	+10.1

FULL FAITH AND CREDIT DEBT

	California		U.S.	
	Amount	% Change	Amount	% Change
1980-81	$6,186,000,000	---	$52,582,000,000	---
1981-82	4,124,000,000	-33.3	51,507,000,000	-2.0
1982-83	4,293,000,000	+4.1	55,078,000,000	+6.9
1983-84	4,355,000,000	+1.4	57,349,000,000	+4.1
1984-85	4,780,000,000	+9.8	60,432,000,000	+5.4

Source: U.S. Department of Commerce, Bureau of the Census, Government Finances.

B. CONSTITUTIONAL AND STATUTORY AUTHORITY

A draft survey of the states conducted by the National Association of State Treasurers indicates that most constitutional or statutory provisions relating to general obligation debt specify limits or caps on the total amount of debt which may be issued or outstanding. Tables 17 and 18 below summarize the legal provisions found in other states with respect to state general obligation bonds, while Tables A-2 and A-3 (on pages A-8 and A-9) list each of the 50 states by the type of limits and approvals for general obligation bonds.

Five states prohibit or do not expressly authorize general obligation debt. The five states are Colorado, Kansas, Indiana, Missouri, and South Dakota.

Although California has no constitutional general obligation debt limits per se, each general obligation bond statute contains a limit on the total amount that may be issued for each specific bond program.

Table 17

SUMMARY OF LIMITS ON THE AMOUNT OF GENERAL OBLIGATION BONDS WHICH MAY BE ISSUED OR OUTSTANDING

Type of Limit	Number of States
Constitutional	21
Statute	6
Both Constitutional and Statute	7
No Limit	8
Unknown	8

Table 18

SUMMARY OF STATE APPROVAL PROCESSES FOR GENERAL OBLIGATION BONDS

Approval Process	Number of States
Referendum Only	8
Legislation Only	8
Both Referendum and Legislation	15
Constitutional Amendment	2
Governor	1
Legislation and Commission	2
Commission	2
Not Authorized	5
Unknown	7

The following is a summary of the type of dollar limits on state general obligation bonds in effect for selected states with constitutional or statutory limits.

- <u>Percentage limits on debt service as a percent of revenue</u>

  - 10.0 percent of prior year net revenue (Georgia);
  - 18.5 percent of average of three years general fund revenue (Hawaii);
  - 3.0 percent of general revenue (Minnesota);
  - 1.75 times the previous five-year average of state revenue (Pennsylvania);
  - 5.0 percent of revenue of previous fiscal year (South Carolina); and
  - 7.0 percent of three-year average of general state revenues (Washington).

- <u>Absolute dollar limits on outstanding debt</u>

  - $2,000,000 without voter approval (Idaho);
  - $6,456,000 (Illinois); and
  - $2,000,000 (North Dakota).

- <u>Percentage limits on outstanding debt</u>

  - General obligation debt limited to 4.5 times the previous year's tax receipts (Connecticut);
  - State commission establishes affordability guidelines each year (Maryland);
  - General obligation bonds limited to amount which specific revenues can amortize (Tennessee);
  - Total limited to 1.5 percent of value of taxable property, currently $752,000,000 (Utah);
  - General obligation bonds revenue debt cannot exceed 1.15 times average annual revenues from three previous fiscal years (Virginia); and
  - Limited to 5.0 percent of full market value of taxable property (Wisconsin).

- <u>Limits on purposes</u>

  - Capital outlay only (Louisiana) and
  - Capital facilities, land, equipment, veterans mortgages (Wisconsin).

C. DEBT MANAGEMENT POLICIES

Selected states were contacted to determine the mechanism used to guide the use of general obligation bonds. Of the total contacted, seven states are rated AAA (Aaa) by both Moody's and Standard & Poor's rating agencies. Here, the primary objective was to ascertain the existence of implicit or explicit debt management policies which may contribute to a AAA (Aaa) rating.

The remaining 12 states contacted were selected because they have more than $1,000,000,000 in outstanding state general obligation debt, they were considered comparable to California in terms of population or economic strength, they were suggested by the rating agencies, or they are rated AAA (Aaa) by one of the rating agencies.

1. AAA States

In an effort to determine whether any special policies might contribute to a AAA (Aaa) rating, staff contacted the State Treasurer's office of Maryland, Missouri, New Jersey, North Carolina, South Carolina, Utah, and Virginia.

Topics and issues covered in the telephone survey included identification of any formal or informal policies regarding:

- limits or caps on amounts of general obligation debt approved or outstanding;
- use of fiscal impact factors such as debt service levels to determine "appropriate" levels of debt;
- use of availability of revenues to determine whether debt financing or pay-as-you-go financing should be used; and
- appropriate or approved uses of proceeds.

Results are summarized in Table 19 on pages 46 and 47.

Except for New Jersey, the AAA-rated states are not readily comparable to California in that they appear to be infrequent issuers of state general obligation bonds. There were no discernible policies other than the very conservative use of state general obligation bonds for any purpose.

Table 19

SUMMARY OF GENERAL OBLIGATION DEBT MANAGEMENT POLICIES OF STATES RATED AAA/Aaa BY STANDARD & POOR'S AND MOODY'S RATING AGENCIES

State	Approval Mechanism	Limits on Amount	Formal Policies	Typical Purposes	Current Outstanding General Obligation Debt
MARYLAND	Legislation	None	Debt Affordability Committee desires to limit total general obligation debt to 3.2% of personal income; debt service limited to 8% of general fund revenues.	Various	$2.1 billion
MISSOURI	Constitutional amendment, approved by referendum	None	None	Water pollution control; state buildings	$309 million
NEW JERSEY	Referendum	1% of total appropriations	None; general obligation bonds are reviewed by Budgeting and Planning Commission for consistency with capital improvement plans	Roads, bridges, prisons hazardous waste, shore protection	$3 billion
NORTH CAROLINA	Referendum; Legislature may approve new debt up to 2/3's of principal retired biennium	None	State looks at what rating agencies consider, i.e., debt and other fiscal indicators	Transportation, economic development	$1 billion

Table 19 (continued)

SUMMARY OF GENERAL OBLIGATION DEBT MANAGEMENT POLICIES OF STATES RATED AAA/Aaa BY STANDARD & POOR'S AND MOODY'S RATING AGENCIES

State	Approval Mechanism	Limits on Amount	Formal Policies	Typical Purposes	Current Outstanding General Obligation Debt
SOUTH CAROLINA	Legislation	Debt service cannot exceed 5% of previous fiscal year's revenues	None	Government facilities; education	$637.5 million
UTAH	Legislation	1.5% of total property value; $723 million authorized	None; process is "market-driven"	Public buildings, higher education, pollution control improvements.	$281 million
VIRGINIA	Referendum for straight general obligation bonds	Voter-approved: 1.5 times the average annual tax revenue for three previous years; Double-barrel: general obligation bonds backed by revenues; no voter approval required	No formalized policies; market-driven process	Public facilities, transportation, education	$78 million general obligation; $350 million double-barrel

Source: California Debt Advisory Commission, August 31, 1987

While New Jersey has no formal debt management policies, the State is attempting to link capital needs with its bonding activity. The State has generally used general obligation bonds for such purposes as roads, bridges, correctional facilities, hazardous waste and pollution control facilities. New Jersey recently approved a general obligation bond issue for shoreline protection and technology commercialization.

According to a New Jersey official, there are many tangible and intangible factors that have resulted in a "good, solid AAA rating." In 1975, the State established the Capital Planning Commission to review appropriations for capital projects and all proposals for State bond authorizations. The Commission's focus is primarily on reviewing the budget to confirm that debt service for proposed projects can be met. Additional factors include sound administration and management of the capital planning budgeting process.

2. Other Selected States

The debt management policies of the remaining 12 states reviewed range from adopted policies with specific limits to very informal monitoring of the impact of additional general obligation debt on standard debt indicators.

Table 20 on pages 49 through 51 summarizes the debt management practices of those states. Two states, Minnesota and Texas, have adopted widely divergent policies. Texas has a "pay-as-you-go" policy toward capital expenditures with the State constitution limiting general obligation bonds to five purposes. In contrast, Minnesota has adopted very specific targets as guidelines for debt financing. These guidelines are presented in the annual State budget.

Most of the states contacted indicated that general obligation bond debt is used to leverage their available resources, by using long-term debt to finance assets with long lives. In addition, representatives of the active states cite the trade-off that sometimes occurs between an AAA (Aaa) rating and the need to address serious and basic capital improvement or capital investment problems.

Table 20

SUMMARY OF GENERAL OBLIGATION DEBT MANAGEMENT POLICIES OF SELECTED STATES

State	Approval Mechanism	Limits on Amount	Formal Policies	Typical Purposes	Current Outstanding General Obligation Debt
ARKANSAS	Legislation/ Referendum	Limited to $250 million outstanding; State can issue $15 million every two years	None	Water/sewer conservation districts	One $15 million issue since 1960
FLORIDA	Legislation/ Referendum; Voters may also initiate	None	Designated revenue earmarked for each issue; Required coverage specified for each issue; full, faith credit pledge activated only if revenues and coverage are inadequate	Education; pollution control; roads; toll bridges	$3.5 billion for full faith and credit debt
GEORGIA	Approval by legislation through appropriation for debt service in annual state budget	None	None; legislature appropriates debt service for maximum amount of bonds to be issued	Public buildings; prisons; highways; hospitals; loans for local water/sewer project	$1.96 billion
ILLINOIS	Legislation	General Assembly sets amounts by purpose annually	None; debt burden indicators are shown in annual budget	Corrections; recreational facilities; State and local transportation; coal resource development	$3.8 billion
MAINE	Legislation/ Referendum (Majority vote for both)	None	None; "rule of thumb" limits annual issuance to seven percent of general fund revenues	Schools; state highways; removal of asbestos in state buildings; acquisition of land for park development	$296 million

Table 20 (continued)

SUMMARY OF GENERAL OBLIGATION DEBT MANAGEMENT POLICIES OF SELECTED STATES

State	Approval Mechanism	Limits on Amount	Formal Policies	Typical Purposes	Current Outstanding General Obligation Debt
MASSA-CHUSETTS	Legislation (2/3's vote)	None	None; State monitors debt ratios to ensure that only prudent amount of authorized but unissued debt is tapped in any one year	Capital outlay for State operations; State grants to local governments for capital improvements	$3.9 billion
MINNESOTA	Legislation	None	Since 1979, Governor's policy: - Transfers to debt service fund cannot exceed 3% of net nondedicated revenue; - Ratio of G.O. debt to personal income cannot exceed 2.5%; - Ratio of all debt of all State entities cannot exceed 3.5%. (not always met)	Pollution control; education; State and local transportation; corrections	$1.1 billion
NEW YORK	Legislation/ Referendum	None	None; State considers impact of additional debt on affordability; State is attempting to coordinate use of COPs by State agencies	Various governmental purposes	$3.6 billion

Table 20 (continued)

SUMMARY OF GENERAL OBLIGATION DEBT MANAGEMENT POLICIES OF SELECTED STATES

State	Approval Mechanism	Limits on Amount	Formal Policies	Typical Purposes	Current Outstanding General Obligation Debt
OHIO	Referendum/constitutional amendment; Coal and highway bonds authorized by legislation; Special obligations authorized by Ohio Public Facilities Commission and Ohio Building Authority	$500 million outstanding for highway bonds; $100 million outstanding for coal development; $2.7 billion may be issued for specific purposes authorized by the voters	None; political process sets policy on uses for for special obligations; informal policy limits debt service to five per-cent of revenues	Highways; coal development; Special obligations: higher education; mental health; prisons; public buildings; parks	$350 million in highway bonds; $48.1 million in coal development; $337 million in other general obligation
OKLAHOMA	Legislative Resolution/Referendum	Constitution requires $90 million in debt service fund	None	G.O. funded IDB's	$5-6 million
TENNESSEE	Legislation	None; first year's debt service must be appropriated and available	None; earmarked revenues cannot be less than 150% of proposed debt service.	State-owned capital projects only; correctional facilities; State-owned educational institutions	$750 million
TEXAS	Legislation/ Referendum	None	"Pay as you go," Bond Review Board has been established recently to develop policies and coordinate issuance	Veterans housing; water facilities; parks; university facilities; all self-funding	

Source: California Debt Advisory Commission, August 31, 1987

D. USE OF GENERAL OBLIGATION BOND PROCEEDS NATIONWIDE

The final component of this section compares California with other states in terms of the use of proceeds of general obligation bonds issued from 1983 through 1986.

Using data from the Securities Data Corporation and IDD Information Services/Public Securities Association the total volume of state general obligation bonds was categorized by purpose from 1983 through 1986 for 40 of the 50 states. Table 21 on page 53 presents general obligation bonds issued by purpose for the 40 states studied for the years 1983 through 1986. (Information on the other ten states was not available from these data sources.)

The information regarding the use of proceeds of general obligation debt is somewhat limited due to the manner in which it is reported by states themselves. Many states, including California, issue large composite general obligation debt issues for multiple purposes. These issues are reported as "other" purposes to the private data sources because the use of proceeds is not confined to one purpose.

In an effort to refine the "other" category, official statements from the largest state issuers in the "other" category were reviewed. Where possible, the information contained in the official statements was used to recalculate the dollar amount, number of issues and percentage of proceeds devoted to each category, thus reducing the amount categorized as "other."

In addition, the data includes short-term debt, such as bond anticipation notes and tax and revenue anticipation notes, if it is considered to be general obligation debt by the state issuer. The data does not include revenue bonds or debt issued by state financing authorities.

1. Overview of General Obligation Debt Purposes

The data summarized for 1983 through 1986 divides debt issuance into nine purpose categories: cash-flow, capital improvements, education, housing, transportation, parks, pollution control, water/sewer/gas/energy, and other.

Cash-flow general obligation debt was the single largest purpose category in 1983. The "other" category was largest from 1984 through 1986.

All the general obligation debt issued by 18 of the 40 states studied was classified as "other" in 1983. The same holds true for 17 of 40 states in 1984, and 20 of 40 states in 1985 and 1986.

Table 21

STATE GENERAL OBLIGATION DEBT, 1983-1986
BY PURPOSE FOR FORTY OF THE FIFTY STATES[1]

Purpose	1983	1984	1985	1986
CASH-FLOW	$7,400,000,000	$5,700,000,000	$6,600,000,000	$6,100,000,000
CAPITAL IMPROVEMENTS[2]	85,000,000	325,000,000	330,000,000	734,505,750
EDUCATION	257,000,000	389,070,000	269,920,000	332,980,000
HOUSING	464,920,000	1,133,510,000	1,527,770,000	975,683,450
TRANSPORTATION[3]	288,740,000	610,815,000	356,000,000	1,351,665,000
PARKS	100,820,000	65,400,000	120,600,000	161,725,000
POLLUTION CONTROL	145,600,000	125,705,000	137,320,000	326,816,221
WATER/SEWER/GAS/ENERGY	463,080,000	286,750,000	243,500,000	464,522,777
OTHER[4]	5,323,390,000	6,311,220,000	7,160,610,000	7,733,939,600
TOTAL	$14,528,550,000	$14,947,470,000	$16,745,720,000	$18,181,837,798

1The ten states not included in this table are Arizona, Delaware, Indiana, Kansas, Kentucky, Nebraska, Oklahoma, South Dakota, West Virginia, and Wyoming.

2Includes governmental facilities, correctional facilities, and economic development.

3Includes mass transportation, toll roads, and other transportation facilities.

4Reported as "other" purposes to private data sources; assumed to be composite multiple purpose issues.

Source: Securities Data Company, Inc., California Debt Advisory Commission, August 31, 1987

Housing ranked third in general obligation debt issued in 1983 through 1985. Transportation ranked third in 1986. Capital improvements was the smallest purpose category in 1983, and parks was the smallest purpose category in 1984 through 1986.

2. General Obligation Issuance by State, 1983-1986

The largest state issuer in terms of dollar volume in 1983 was California. New York was largest in 1984 through 1986, and second largest in 1983. California ranked second in 1984 through 1986. Pennsylvania was third largest for two of the four years, 1983 and 1984. Oregon was third largest in 1985, and Texas was third in 1986.

Three states issued general obligation debt only once over the four year period: Arkansas issued $15,000,000 in 1985; Alaska issued $78,000,000 in 1983; and Iowa issued $463,000,000 in 1986.

The most frequent issuers in the market included Oregon, with 17 issues in 1985, California with ten in both 1983 and 1984, and Massachusetts with ten in 1984.

Table A-1

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Percent of Vote Against
Greene-Hughes School Building Lease-Purchase Bond Law of 1986	11/04/86	$800,000,000	60.7%	39.3%
New Prison Construction Bond Act of 1986	11/04/86	500,000,000	65.3%	34.7%
California Safe Drinking Water Bond Law of 1986	11/04/86	100,000,000	78.7%	21.3%
Higher Education Facilities Bond Act of 1986	11/04/86	400,000,000	59.5%	40.5%
Veterans Bond Act of 1986	06/03/86	850,000,000	75.6%	24.4%
Community Parklands Act of 1986	06/03/86	100,000,000	67.3%	32.7%
Water Conservation and Water Quality Bond Law of 1986	06/03/86	150,000,000	74.1%	25.9%
County Correctional Facility Capital Expenditure Bond Act of 1986	06/03/86	495,000,000	67.2%	32.8%
Clean Water Bond Law of 1984	11/06/84	325,000,000	72.9%	27.1%
State School Building Lease-Purchase Bond Law of 1984	11/06/84	450,000,000	60.7%	39.3%
Hazardous Substance Cleanup Bond Act	11/06/84	100,000,000	72.0%	28.0%
California Safe Drinking Water Bond Law of 1984	11/06/84	75,000,000	73.5%	26.5%
Veterans Bond Act of 1984	11/06/84	650,000,000	66.3%	33.7%
Senior Center Bond Act of 1984	11/06/84	50,000,000	66.7%	33.3%
County Jail Capital Expenditure Bond Act of 1984	06/05/84	250,000,000	58.8%	41.2%
New Prison Construction Bond Act of 1984	06/05/84	300,000,000	57.8%	42.2%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Percent of Vote Against
California Park and Recreational Facilities Act of 1984	06/05/84	$370,000,000	63.2%	36.8%
Fish and Wildlife Habitat Enhancement Act of 1984	06/05/84	85,000,000	64.0%	36.0%
State School Building Lease-Purchase Bond Law of 1982	11/02/82	500,000,000	50.5%	49.5%
County Jail Capital Expenditures Bond Act of 1981	11/02/82	280,000,000	54.3%	45.7%
Veterans Bond Act of 1982	11/02/82	450,000,000	67.1%	32.9%
Lake Tahoe Acquisitions Bond Act	11/02/82	85,000,000	52.9%	47.1%
First-Time Home Buyers Bond Act of 1982	11/02/82	200,000,000	53.8%	46.2%
New Prison Construction Bond Act of 1981	06/08/82	495,000,000	56.1%	43.9%
Parklands Acquisition and Development Program	11/04/80	285,000,000	51.7%	48.3%
Lake Tahoe Acquisitions Bond Act of 1980	11/04/80	85,000,000	48.8%	51.2%
Parklands and Renewable Resources Investment Program	06/03/80	495,000,000	47.0%	53.0%
Veterans Bond Act of 1980	06/03/80	750,000,000	65.5%	34.5%
Veterans Bond Act of 1978	11/07/78	500,000,000	62.3%	37.7%
State School Building Aid Bond Law	06/06/78	350,000,000	35.0%	65.0%
Clean Water and Water Conservation Bond Act of 1978	06/06/78	375,000,000	53.5%	46.5%
Housing Finance Bond Law of 1975	11/02/76	500,000,000	42.8%	57.2%
Nejedly-Hart State, Urban, and Coastal Park Bond Act of 1976	11/02/76	280,000,000	51.5%	48.5%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Against
Residential Energy Conservation Bond Law	11/02/76	$25,000,000	41.4%	58.6%
State School Building Lease-Purchase Bond Law of 1976	06/08/76	200,000,000	47.3%	52.7%
Veterans Bond Act of 1976	06/08/76	500,000,000	62.5%	37.5%
California Safe Drinking Water Bond Law of 1976	06/08/76	175,000,000	62.6%	37.4%
Bonds to Provide Public Community College Facilities	06/08/76	150,000,000	43.9%	56.1%
State School Building Aid and Earthquake Reconstruction and Replacement Bond Law of 1974	11/05/74	150,000,000	60.1%	39.9%
State Beach, Park, Recreational, and Historical Facilities Bond Act of 1974	06/04/74	250,000,000	59.9%	40.1%
Clean Water Bond Law of 1974	06/04/74	250,000,000	70.5%	29.5%
Veterans Bond Act of 1974	06/04/74	350,000,000	72.3%	27.7%
Bonds to Provide Public Community College Facilities	11/07/72	160,000,000	56.9%	43.1%
Bonds to Provide Health Science Facilities	11/07/72	155,900,000	60.0%	40.0%
Veterans Bond Act of 1971	06/06/72	250,000,000	65.5%	34.5%
State School Building Aid and Earthquake Reconstruction and Replacement Bond Law of 1972	06/06/72	350,000,000	47.9%	52.1%
Clean Water Bond Law of 1970	11/03/70	250,000,000	75.4%	24.6%
Recreation, Fish, and Wildlife Enhancement Bonds	11/03/70	60,000,000	56.7%	43.3%
Bonds to Provide University of California Health Science Facilities	06/02/70	246,300,000	45.0%	55.0%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of VOote For	Against
Bonds to Provide State College, University, and Urban School Facilities	11/05/68	$250,000,000	44.6%	55.4%
Veterans Bond Act of 1968	06/04/68	200,000,000	61.8%	38.2%
Bonds to Provide Junior College Facilities	06/04/68	65,000,000	56.6%	43.4%
Bonds to Provide State College and University Facilities	11/08/66	230,000,000	56.1%	43.9%
State School Building Aid Bond Law of 1966	06/07/66	275,000,000	60.6%	39.4%
State Beach, Park, Recreational, and Historical Facilities Bond Act of 1964	11/03/64	150,000,000	62.4%	37.6%
Bonds to Provide State College, Junior College and University Facilities, and to Provide Funds to Meet the Building Needs of the State, Including Facilities to Care for Mentally Retarded and Mentally Ill and Narcotics Control, Correctional and Forest Fire Fighting Facilities	11/03/64	380,000,000	64.9%	35.1%
State School Building Aid Bond Law of 1964	11/03/64	260,000,000	69.4%	30.6%
Bonds to Provide State College, Junior College and University Facilities; to Provide Facilities to Care for Mentally Retarded and Mentally Ill and to Provide Narcotics Control, Correctional and Forest Fire Fighting Facilities	11/06/62	270,000,000	66.2%	33.8%
State School Building Aid Bond Law of 1962	06/05/62	200,000,000	59.4%	40.6%
Veterans Bond Act of 1962	06/05/62	250,000,000	50.3%	49.7%
State Construction Program Bond Act of 1962	06/05/62	270,000,000	37.3%	62.7%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Against
Housing for the Aged and Physically Handicapped	06/05/62	$100,000,000	36.6%	63.4%
State Park and Recreation Bond Act	06/05/62	150,000,000	47.3%	52.7%
California Water Resources Development Bond Act	11/08/60	1,750,000,000	51.5%	48.5%
Veterans Farm and Home Bonds	06/07/60	400,000,000	64.9%	35.1%
School Bonds	06/07/60	300,000,000	71.8%	28.2%
Veterans Bond Act of 1958	11/04/58	300,000,000	73.9%	26.1%
School Bonds	11/04/58	220,000,000	74.2%	25.8%
State Construction Progam Bonds	11/04/58	200,000,000	63.7%	36.3%
Harbor Development Bonds	11/04/58	60,000,000	56.5%	43.5%
Veterans Bond Act of 1956	11/06/56	500,000,000	80.4%	19.6%
School Bonds	11/06/56	100,000,000	82.3%	17.7%
State Construction Program Bonds	11/06/56	200,000,000	77.9%	22.1%
Veterans Bond Act of 1954	11/02/54	175,000,000	79.4%	20.6%
School Bonds	11/02/54	100,000,000	80.1%	19.9%
Veterans Farm and Home Bonds	11/04/52	150,000,000	85.7%	14.3%
School Bonds	11/04/52	185,000,000	76.6%	23.4%
Veterans Farm and Home Bonds	06/06/50	100,000,000	72.0%	28.0%
School Bonds	11/08/49	250,000,000	72.8%	27.2%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Percent of Vote Against
Veterans Bond Act of 1946	11/05/46	$100,000,000	79.6%	20.4%
Veterans Bond Act of 1943	11/07/44	30,000,000	87.7%	12.3%
State Building Bond Act of 1935	08/13/35	13,950,000	46.7%	53.3%
Veterans Welfare Bond Act of 1933	11/06/34	30,000,000	60.8%	39.2%
Unemployment Relief Bonds	11/06/34	24,000,000	71.0%	29.0%
Unemployment Relief Bonds	06/27/33	20,000,000	73.6%	26.4%
Veterans Welfare Bond Act	11/04/30	20,000,000	75.9%	24.1%
California Olympiad Bond Act	11/06/28	1,000,000	72.9%	27.1%
California State Park Bond Act	11/06/28	6,000,000	73.8%	26.2%
Grade Separation Bonds	11/06/28	10,000,000	38.8%	61.2%
Veterans Welfare Bond Act of 1925	11/02/26	20,000,000	76.3%	23.7%
Bonds for State and University Buildings	11/02/26	8,500,000	67.6%	32.4%
Water and Power Bonds (Initiative)	11/02/26	500,000,000	27.4%	72.6%
Veterans Welfare Bond Act of 1921	11/07/22	10,000,000	68.5%	31.5%
Land Settlement Bond Act	11/07/22	3,000,000	49.2%	50.8%
Water and Power Bonds (Initiative)	11/07/22	500,000,000	29.0%	71.0%
Highway Bonds (Initiative)	11/02/20	40,000,000	58.3%	41.7%

Table A-1 (continued)

SUMMARY OF GENERAL OBLIGATION BOND BALLOT MEASURES, 1900-1986

Bond Act Name	Date of Election	Amount of Bond Issue	Percent of Vote For	Percent of Vote Against
State Highway Act of 1915	11/07/16	$15,000,000	79.8%	20.2%
University of California Building Bond Act	11/03/14	1,800,000	63.3%	36.7%
State Building Bond Act (Sacramento)	11/03/14	3,000,000	52.4%	47.6%
State Building Bond Act (San Francisco)	11/03/14	1,000,000	53.9%	46.1%
State Fairgrounds Bonds	11/03/14	750,000	46.3%	53.7%
Los Angeles State Building Bonds (Initiative)	11/03/14	1,250,000	47.2%	52.8%
San Francisco Harbor Improvement Act of 1913	11/03/14	10,000,000	70.9%	29.1%
San Francisco Harbor Improvement Act of 1909	11/08/10	9,000,000	75.7%	24.3%
State Highway Act	11/08/10	18,000,000	53.7%	46.3%
India Basin Act	11/08/10	1,000,000	61.0%	39.0%
San Diego Seawall Act	11/08/10	1,500,000	64.6%	35.4%
San Francisco Seawall Act	11/03/08	2,000,000	48.8%	51.2%
India Basin Act	11/03/08	1,000,000	44.5%	55.5%
San Francisco Seawall Act	11/08/04	2,000,000	81.7%	18.3%
TOTAL		**$24,645,950,000**		

Note: A $40,000,000 ballot measure for State Highway Bonds was considered and approved in 1919. It is not included here because it was superceded by a subsequent ballot measure.

Source: California Secretary of State's Office, California Debt Advisory Commission, August 31, 1987

Table A-2

COMPARISON OF STATE CONSTITUTIONAL OR STATUTORY LIMITS ON THE AMOUNT OF GENERAL OBLIGATION BONDS WHICH MAY BE ISSUED OR OUTSTANDING

Constitutional Limit	Statutory Limit	Constitutional/ Statutory Limits	No Limit	Unknown
Arizona	Connecticut	Arkansas	Alabama	Iowa
Hawaii	Delaware	Colorado	Alaska	Kansas
Idaho	Louisiana	Florida	California	Maine
Indiana	Maryland	Georgia	Illinois	Massachusetts
Kentucky	Tennessee	Nevada	Minnesota	Mississippi
Michigan	Vermont	Washington	Montana	Nebraska
Missouri		Wisconsin	New Hampshire	New York
New Jersey			Rhode Island	Oklahoma
New Mexico				
North Carolina				
North Dakota				
Ohio				
Oregon				
Pennsylvania				
South Carolina				
South Dakota				
Texas				
Utah				
Virginia				
West Virginia				
Wyoming				

Source: National Association of State Treasurers, Survey Draft, August 31, 1987

Table A-3

COMPARISON OF STATE APPROVAL PROCESSES FOR GENERAL OBLIGATION BONDS

Referendum	Legislation	Referendum/ Legislation	Constitutional Amendment	Governor	Legislation and Commission	Commission	Not Authorized	Unknown
Alabama	Delaware	California	Oregon	Montana	Connecticut	Louisiana	Colorado	Arizona
Alaska	Georgia	Florida	Texas		Wisconsin	North Dakota	Indiana	Massachusetts
Arkansas	Hawaii	Maine					Kansas	Nebraska
Iowa	Idaho	Michigan					Missouri	Nevada
Kentucky	Illinois	New Jersey					South Dakota	New York
New Mexico	Maryland	North Carolina						Oklahoma
Rhode Island	Minnesota	Pennsylvania						Washington
West Virginia	Mississippi	Virginia						
		New Hampshire						
		Ohio						
		South Carolina						
		Tennessee						
		Utah						
		Vermont						
		Wyoming						

Source: National Association of State Treasurers, Survey Draft, August 31, 1987