

**Fiscal Year 2011 Report on Debt Management
To the
Public Finance Management Board**

September 2012

**State of Rhode Island
And Providence Plantations**

OFFICE OF THE GENERAL TREASURER

GINA M. RAIMONDO
GENERAL TREASURER

Table of Contents



Section	Page
1. 2011 Findings _____	1
2. Rhode Island State Debt _____	8
3. Classification of State Debt _____	10
4. Debt Policies and Practices _____	19
5. Recommended Priorities and Issues for 2012 and 2013 _____	25

Exhibits

- A. Schedule of Tax-Supported Debt
- B. Summary of Debt Issuances
- C. Credit Rating Reports

September 2012

Members of the Rhode Island Public Finance Management Board

Mr. Richard Licht, Director of Administration, State of Rhode Island
The Honorable A. Ralph Mollis, Secretary of State, State of Rhode Island
Mr. W. Lincoln Mossop, Jr., Public Member
Mr. Robert A. Mancini, Public Member
Mr. Edward F. Yazbak, Public Member
Mr. Steven Filippi, Public Member
Mr. Thomas M. Bruce, III, Public Member

Dear Members of the Board:

I hereby submit the fiscal year 2011 Debt Management Report for the State of Rhode Island and Providence Plantations (the “State” or “Rhode Island”). This report once again demonstrates the continued importance of closely monitoring the State’s debt management efforts to maintain and improve the State’s credit worthiness.

In recent years, debt management has been a top priority of the State resulting in significant improvement in several long-term debt trends. As recently as 2001, Rhode Island’s debt burden was the 7th highest nationally according to Moody’s Investors Service. The 2011 Moody’s State Debt Medians show that Rhode Island’s ranking has dropped to 12th for debt per capita and 14th for debt as a percentage of personal income.

Net tax supported debt totaled \$1.76 billion at the close of FY 2011 and current Budget Office forecasts project the State’s debt level to increase slightly to \$1.77 billion by FY 2016.

A major responsibility of the Treasurer’s Office and the PFMB is to monitor State debt ratios and to preserve and enhance Rhode Island’s credit ratings and presence in the financial markets. Maintenance of prudent debt ratios and securing positive ratings from the credit rating agencies will allow Rhode Island to obtain financing at the lowest possible interest rates. To maintain its credit ratings at an appropriate level, the State must continue to make fiscal responsibility a top priority.

Rhode Island's fiscal situation was characterized as "strained" by the three major credit rating agencies prior to the national recession. The economic downturn and the global financial crisis had a serious impact on the financial flexibility of all the states that was felt for several fiscal years.

The State's credit rating agencies highly scrutinized budgetary decisions during this challenging time. Maintenance of the State's "Double A" category ratings is more important now than ever before, as credit spreads reached their widest levels in decades in 2008 and have remained above historical levels. The ability to access the capital markets has become increasingly challenging for issuers such as the State. The demise of the municipal bond insurance industry, coupled with the credit squeeze and the notable absence of several major investment banking firms will continue to have an impact on the State as it seeks to finance its capital needs. Navigating these elements will be a significant priority for the State to insure continued access to capital at affordable levels.

According to State Budget Office projections, it appears that the ratio of debt service to revenues will remain within the PFMB's guideline of 7.5%. The economic climate of the past three fiscal years has resulted in anemic revenue growth. Since the State must continue to issue debt to fund its capital needs, the increased debt service is a growing percentage of a smaller revenue base. At this time, we do not recommend revision of the guideline, but careful monitoring as noted above.

Sincerely,

Gina M. Raimondo
General Treasurer

SECTION 1

2011 Findings

The 2011 Report includes the following:

- Φ Analysis of current State debt position and trends.
- Φ Status report on the implementation of debt management methods and policies.
- Φ Evaluation of projected new debt issuance in compliance with the Public Finance Management Board's ("PFMB") adopted Credit Guidelines.
- Φ Information about outstanding debt issued by State-related agencies and summary information on local government debt position and trends.

The principal findings of this report are summarized below.

Rhode Island's Debt Burden Remains Moderately High

Rhode Island's debt levels continue to improve, but are still relatively high, as evidenced by the following statistics provided by a Moody's Investor Service State Debt Medians Report, May 2012 and the FY13 Capital Budget:

- Rhode Island ranks 14th highest among all states in Net Tax-Supported Debt as a percent of personal income, at 4.7% (based on Moody's calculations and 2010 personal income).
- Rhode Island ranks 12th highest among all states in Net Tax-Supported Debt per capita at \$1,997 (based on Moody's calculations).
- Net Tax-Supported Debt increased annually by 2.1% from FY07 – FY11. Personal income growth for the same period was 2.0%.
- In FY11 the general obligation debt decreased at a rate of 6.1% over FY10. From FY07 – FY11 general obligation debt increased at a rate of 3.5%.

Over the last four years, Net Tax-Supported Debt increased by \$138.0 million, from \$1.62 billion at FY07 to \$1.76 billion at FY11. Current Tax-Supported Debt of \$1.76 billion represents a decrease of 6.6% from \$1.88 billion at FY10.

According to the FY13 Capital Budget, the State's outstanding Net Tax-Supported Debt (includes adjustment for agency payments) is projected to remain stable at \$1.77 billion for FY16. This projection assumes the issuance of no new Tax Supported Debt during this period other than as projected in the Capital Budget.

The Capital Budget for FY13 also indicates that State general obligation debt will decrease at a compound annual growth rate of 0.4% from \$1,119.4 million at FY12 to \$1,103.8 million at FY16. The Economic Development Corporation debt will increase at a compound annual growth rate of 3.6%. During the same period, it is estimated that capital leases will decrease at a compound annual growth rate of 9.8% and Convention Center Authority will decrease by 4.4%.

Rhode Island's efforts to improve its debt position continue to be recognized by the municipal credit rating agencies. Pension reform measures that were adopted during the 2005 legislative session contributed to Standard and Poor's upgrade of the State's bond rating from AA- to AA. Protecting the gains made in debt reduction is critical and important to preserving financial flexibility.

In 2010 two of the municipal rating agencies recalibrated municipal ratings. Fitch completed their process in April 2010 and Moody's recalibrated the states in May 2010. Standard & Poor's had been using one rating scale for approximately two years. These actions were in response to the Markets' demand for enhanced comparability between municipal ratings and non-municipal ratings. As a result of recalibration, the General Obligation ratings of the States are higher on the "global" or "corporate" scale than their place on the municipal ratings scale. However, these actions were not viewed as improvements in credit quality or rating upgrades, but as an alignment of municipal ratings with corporate or global equivalents.

In a Special Comment publication dated July 22, 2010, Moody's Investors Service noted that the key drivers of state government credit quality in the near term are;

Reliability of budgets

Revenue forecasts

Risk of double dip recession

Magnitude of structural imbalance

Phase-out of federal stimulus (ARRA) funding

Financial flexibility and availability of reserves

Available liquidity

Extent of long-term liabilities

Exposure to variable rate debt

Political consensus related to spending and benefit levels

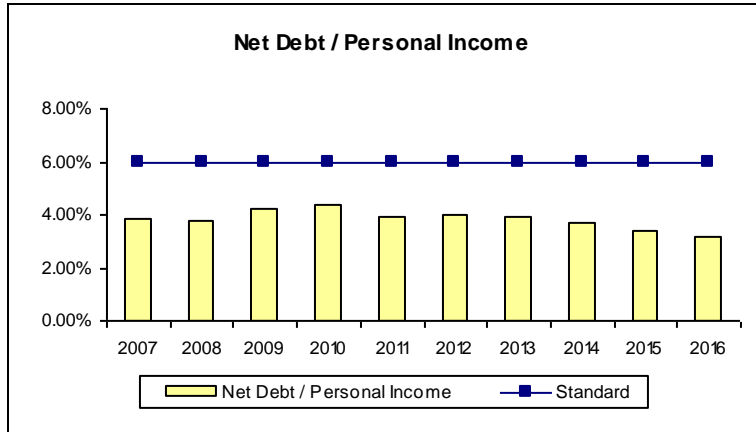
PFMB's Credit Guidelines and Debt Ratio Targets

In recognition of Rhode Island's high debt burden, the PFMB adopted Credit Guidelines recommended in the 1997 report for use in evaluating certain elements of the State's debt. The original Credit Guidelines were adopted after extensive research on State debt trends and a comparative analysis of certain "peer" states with demographic, geographic, and financial characteristics similar to Rhode Island. The Credit Guidelines were intended to be restrictive enough to be relevant in managing debt levels, but flexible enough to allow for the funding of critical infrastructure needs. However, in light of the State's already high debt burden at the time of adoption, the Credit Guidelines did not necessarily represent an "ideal" level of State debt.

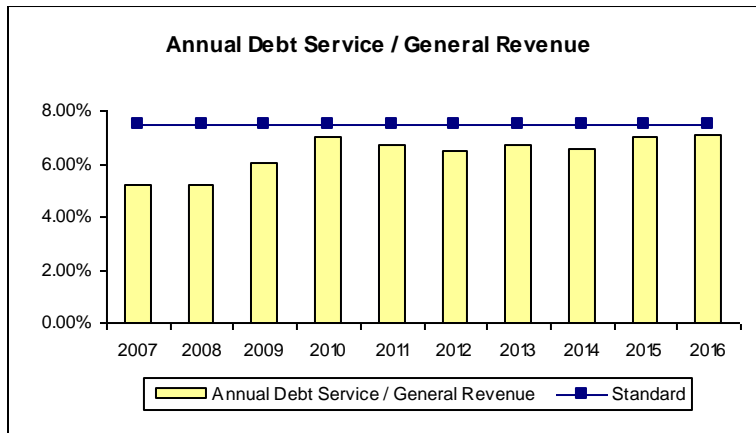
The PFMB approved the following revisions to the Tax-Supported Debt to Personal Income target debt ratios recommended in the 1999 Report on Debt Management. Approved guidelines are as follows:

- ***Credit Guideline 1:*** Tax-Supported Debt to not exceed the target range of 5.0% to 6.0% of personal income, and annual debt service for Tax-Supported Debt to not exceed 7.5% of General Revenues. It is anticipated that fluctuation of this ratio over the long-term will be affected by both variations in personal income levels and debt issuance. The target ranges will continue to be reviewed on an annual basis with consideration given to trends in the State's debt level and upcoming infrastructure projects.
- ***Credit Guideline 2:*** The Board should monitor the total amount of Tax-Supported Debt, State Supported Revenue Debt, and Agency Revenue Debt in relation to the State's personal income.
- ***Credit Guideline 3:*** The Credit Guidelines may be exceeded temporarily under certain extraordinary conditions. If a Credit Guideline is exceeded due to economic or financial circumstances, the Board should request that the Governor and the Legislature recommend a plan to return debt levels to the Guidelines within five years.

The debt projections in this report remain within the Credit Guidelines relating to Net Debt to Personal Income, as the ratio will decline from 4.0% at FY12 to 3.2% at FY16. From FY07 to FY11, Personal Income grew at a rate of 2.0%, while Net Tax-Supported Debt increased by 2.1%. The combination of lower Personal Income growth and lower debt growth resulted in the Net Debt to Personal Income ratio of 3.9% at FY07 remaining stable at 3.9% for FY11.



Annual Debt Service as a percentage of revenues increased from 5.2% in FY07 to 6.7% in FY11. Projections from FY12 to FY16 indicate compliance with the PFMB's guidelines as the FY12 - FY16 debt service to revenues ratio does not exceed 7.5%.

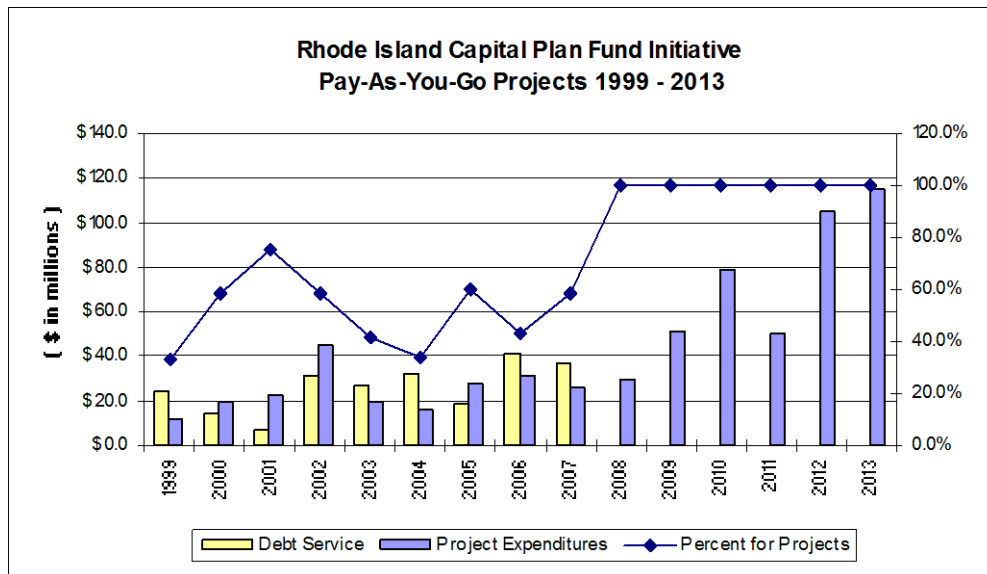


Positive Steps in Debt Administration

Over the years, Rhode Island has made improvements to its debt planning and administration, beginning with the implementation of a formal capital budgeting process and the adoption of the Public Corporation Debt Management Act in 1994 (§RIGL 35-18). The State’s debt load can have a negative impact on the flexibility of the operating budget and limits the State’s ability to meet unanticipated capital financing and economic development needs. Listed below are several initiatives related to debt administration undertaken by the State in recent years.

- 1. Pay-As-You-Go Capital Financing.** During a period of sustained economic expansion from 1998 – 2001, along with improved cash management, the State was able to forego cash flow borrowing, a positive trend in the State’s debt management. However, economic conditions compelled the State to borrow on a short-term basis in 2002, 2003 and 2006 thru 2011. Greater financial flexibility during periods of economic expansion enabled the State to increase the proportion of pay-as-you-go capital spending, which includes using both gas tax funds and funds dedicated to the Rhode Island Capital Fund. [UPDATE ON RICAP]

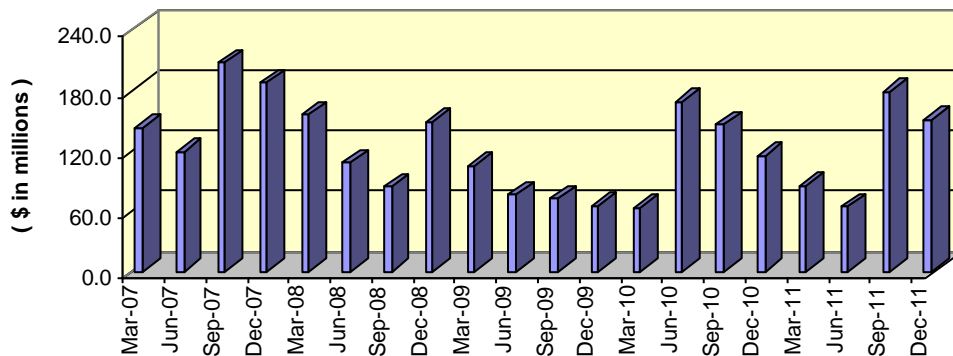
Included in the governor’s recommended FY13 Budget was a \$115.3 million appropriation (\$105.0 million in FY12 which includes funding reappropriations from FY11) for pay-as-you-go capital financing through the Rhode Island Capital Plan Fund. According to the FY13 Capital Budget, 100.0% of the Fund’s resources will be used for capital asset protection projects in FY13.



2. Bond Proceeds Management. The State continues to monitor the issue of unexpended balances of general obligation bond proceeds. Past reports have noted this as an issue of concern. Unexpended proceeds were \$151.1 million as of December 31, 2011 up from \$114.8 million as of December 31, 2010.

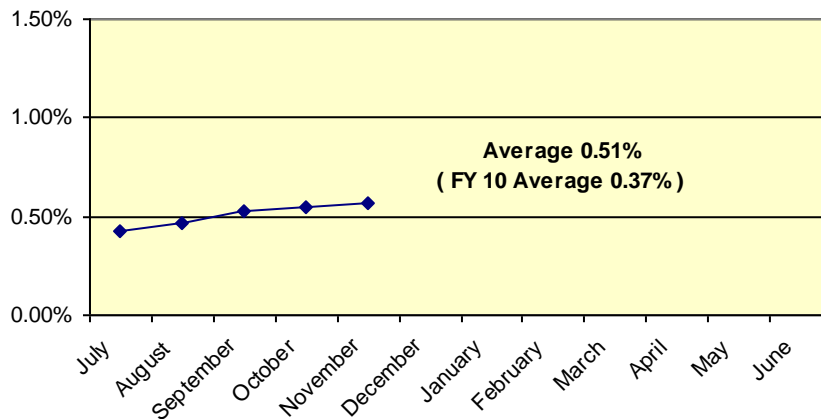
As shown in the chart below, there is a cyclical peak at the end of the second or third quarter, which is indicative of the traditional timing of bond issuance.

Quarterly Balances of Bond Proceeds 3/2007 - 12/2011



3. Variable Rate Debt Obligations Issued. The State was involved in a variable rate financing for McCoy Stadium that was issued by the Economic Development Corporation in July 1998. The floating rate structure offered (1) low initial interest rates, (2) principal structuring flexibility, including prepayment without penalty, and (3) the ability to convert to a fixed rate on one month's notice. The State also issued two series of variable rate bonds in the 1990's that were subsequently refunded by fixed rate bonds. At the time of issuance, the variable rate component improved the match of State assets and liabilities and provided a lower overall cost of capital.

**McCoy Stadium Issue - Series 1998
Monthly Rates
July 2010 - November 2010**



The General Treasurer and the State Budget Office have implemented a policy which restricts the total amount of variable rate exposure to 10% of net tax supported debt outstanding.

In the 2001 session of the RI General Assembly, the Legislature approved a bill proposed by the Treasurer's office to permit the State to enter into interest rate swap agreements with the goal of reducing borrowing costs. This effectively permits the State to convert a fixed rate obligation to a variable rate obligation or vice-versa. The fiscal impact of future transactions is not possible to quantify since any benefit derived from the use of variable rate debt and related interest rate swaps is extremely dependent upon market conditions, the extent to which the investment vehicle is utilized and the specifics of the individual transaction. The State can only enter into such transactions when there are demonstrated savings. To date the State has not utilized interest rate swaps but has provided assistance to various state agencies in analyzing financing alternatives, refinancing variable rate debt and unwinding swaps. The final installment on the McCoy Stadium bonds was made on December 15, 2010, eliminating any State exposure to variable rate debt.

4. **Municipal Debt Report.** The PFMB is also required to report on R.I. local government debt which is a summary of debt issued by cities and towns and other authorities to comply with Section 42-10.1-4. This report will be issued on or before September 30, 2012.

SECTION 2

Rhode Island State Debt

Table 2-1 below is a summary detail statement of outstanding State debt, followed by a brief glossary of terms describing each category of debt.

Table 2-1								
Rhode Island Debt Statement								
(as of June 30, 2011, dollars in millions, principal amount)								
						<u>6/30/2009</u>	<u>6/30/2010</u>	<u>6/30/2011</u>
Tax-Supported Debt								
	General Obligation Bonds					\$ 1,036.2	\$ 1,118.0	\$ 1,049.4
	Capital Leases					267.1	254.7	233.6
	Convention Center Authority					263.8	268.3	259.6
	Economic Development Corporation					286.5	259.9	238.4
	R.I.H.M.F.C. Neighborhood Opportunities Housing Program					13.2	8.4	3.5
	Refunding Bond Authority					6.0	-	-
	Gross Tax-Supported Debt					\$ 1,872.8	\$ 1,909.3	\$ 1,784.5
	Agency Payments					(26.6)	(25.4)	(24.1)
	Net Tax-Supported Debt					\$ 1,846.2	\$ 1,883.9	\$ 1,760.4
State Supported Revenue Debt								
	EDC - Providence Place Mall					30.4	28.6	26.7
	R.I. Housing					285.3	267.3	235.2
	Industrial Recreational Building Authority - Insured							
	Industrial Facilities Corporation					14.1	18.1	20.8
	State Supported Revenue Debt					\$ 329.8	\$ 314.0	\$ 282.7
Agency Revenue Debt								
	Airport Corporation					\$ 327.7	\$ 319.7	\$ 309.7
	Economic Development Corporation					94.4	94.0	97.5
	EDC - GARVEE Bonds, Federally Funded					427.4	400.5	372.3
	R.I. Housing					5.0	5.0	5.0
	Narragansett Bay Commission					444.0	410.1	422.4
	Resource Recovery Corporation					14.8	14.0	13.1
	State University and Colleges					222.6	283.1	276.2
	Turnpike and Bridge Authority					23.6	70.7	69.2
	Water Resources Board					5.8	4.9	4.1
	Agency Revenue Debt					\$ 1,565.3	\$ 1,602.0	\$ 1,569.5
Conduit Debt								
	Clean Water Finance Agency					\$ 602.6	\$ 652.7	\$ 671.2
	Health and Educational Building Corporation					2,377.6	1,793.7	2,574.5
	R.I. Housing					1,293.7	1,445.1	1,416.5
	Industrial Facilities Corporation					89.3	95.3	80.8
	Student Loan Authority					1,046.3	1,331.4	1,026.6
	Water Resources Board					1.0	-	-
	Conduit Debt					\$ 5,410.5	\$ 5,318.2	\$ 5,769.6
Sources: FY 13 Capital Budget and Treasury Survey of R.I. Quasi-Public Corporations.								

Explanation of Categories of Debt

Below is a definition of the four general categories of debt, which are used throughout this report and reflected in Table 2-1 on the previous page. These categories are listed in declining relationship to the State's general credit. To the extent possible, the categories are consistent with the methods credit analysts use in reviewing a state's debt levels. Credit analysts are the professionals who assign credit ratings and recommend and evaluate debt as investments for investors in tax exempt bonds.

Tax-Supported Debt

Tax-Supported Debt is payable from or secured by general taxes and revenues of the State or by specific State collected taxes that are pledged to pay a particular debt. Because of the claim this debt has on the State's credit, this is the most relevant debt figure to State taxpayers.

State Supported Revenue Debt

State Supported Revenue Debt is payable from specified revenues pledged for debt service which are not general taxes and revenues of the State. However, the State provides additional credit support to repay this debt if the pledged revenues are insufficient to meet scheduled debt service requirements. Because of the contingent nature of the State Credit Support, this figure is somewhat less important than Tax Supported Debt. This type of debt includes "moral obligation" debt.

Agency Revenue Debt

Agency Revenue Debt is similar to State Supported Revenue Debt; except that no State credit support is legally pledged for repayment and the assets financed are State owned enterprises that are intended to be supported by internally generated fees and revenues. While this type of debt is not supported by State taxes, the agencies and public corporations responsible for this debt may also have financed some assets with State general obligation debt, thereby indirectly linking such debt to the State.

Conduit Debt

Conduit Debt is issued by a state agency or public corporation on behalf of borrowers which include businesses, health care institutions, private higher education institutions, local governments, and qualified individuals (loans for higher education and housing purposes). No State credit support is provided.

SECTION 3

Classification of State Debt

The Debt Issuers

The electorate of the State and the General Assembly authorize certain State officers, State agencies, and municipalities to issue debt for various purposes. This report uses the terms “issuers” and “debt issuing agencies” to describe any State office, department, corporation, or agency which issues bonds, notes, or other securities. These issuers finance construction and other capital improvements to State buildings; State highways; local water, sewer, and other capital improvement projects; loans to businesses; health care organizations; loans to low and moderate income persons for single family housing and higher education; loans to developers for multifamily housing; and private and public university buildings.

There are currently 15 different State debt issuers that have been authorized to sell various types of obligations. Table 3-1 presents a list of each issuer and the type of debt each has issued.

Table 3-1
State Debt Issuing Agencies

<u>Issuer</u>	<u>Tax-Supported Debt</u>	<u>Revenue Debt (State Credit Support)</u>	<u>Agency Revenue Debt</u>	<u>Conduit Debt</u>
Airport Corporation* (1)			X	
Clean Water Finance Agency				X
Convention Center Authority	X			
Economic Development Corporation	X	X	X	
Health and Education Building Corp.				X
Housing, Mortgage, and Finance Corp.	X	X	X	X
Industrial Facilities Corp.		X		X
Narragansett Bay Commission			X	
Resource Recovery Corporation			X	
State of Rhode Island-Capital Leases	X			
State of Rhode Island-GO Bonds	X			
State Universities and Colleges			X	
Student Loan Authority				X
Turnpike and Bridge Authority			X	
Water Resources Board			X	X

* The State has outstanding general obligation bonds issued on behalf of this agency.

(1) Borrows through the Economic Development Corporation.

Tax-Supported Debt: FY07 to FY11

Tax-Supported Debt includes general obligation bonds and bonds payable from leases which are subject to appropriation from the State's general fund. Credit ratings for this debt are largely dependent on the general fiscal condition of the State, amount of Tax-Supported Debt currently outstanding, the characteristics of the specific tax that is pledged for repayment, and the economic conditions of the State.

Table 3-2 presents the amounts and types of Tax-Supported Debt for the five years ending June 30, 2011 with resulting debt ratios. For FY11, the State's Debt to Personal Income ratio of 3.9% and Debt Service to Revenue ratio of 6.7% were in compliance with the Credit Guideline maximums of 6.0% and 7.5%, respectively. A detailed statement of Outstanding Tax-Supported Debt (actual) as of June 30, 2011 is presented in Appendix A.

Table 3-2
Tax-Supported Debt: Fiscal Years 2007 - 2011
(dollars in millions, principal amount)

Fiscal Years	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>CAGR</u> <u>FY 07 - 11</u>
General Obligation Bonds	\$ 913.5	\$ 997.1	\$ 1,036.2	\$ 1,118.0	\$ 1,049.4	3.5%
Capital Leases	252.6	226.0	267.1	254.7	233.6	-1.9%
Convention Center Authority	280.0	271.0	263.8	268.3	259.6	-1.9%
Economic Development Corp.	147.0	142.6	286.5	259.9	238.4	12.8%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	15.5	18.2	13.2	8.4	3.5	-31.1%
Refunding Bond Authority (1)	42.7	24.2	6.0	-	-	-
Gross Tax-Supported Debt	\$ 1,651.3	\$ 1,679.1	\$ 1,872.8	\$ 1,909.3	\$ 1,784.5	2.0%
Agency Payments	(28.9)	(27.8)	(26.6)	(25.4)	(24.1)	-4.4%
Net Tax-Supported Debt	\$ 1,622.4	\$ 1,651.3	\$ 1,846.2	\$ 1,883.9	\$ 1,760.4	2.1%
Annual Net Tax-Supported Debt Service (2)	\$ 174.8	\$ 185.8	\$ 196.7	\$ 218.2	\$ 212.8	5.0%
Debt Ratios: (3)						
Annual Debt Service / Revenues (7.5%)	5.2%	5.2%	6.0%	7.0%	6.7%	6.7%
Net Debt / Personal Income (5% - 6%)	3.9%	3.8%	4.2%	4.3%	3.9%	0.1%
Net Debt / Capita	\$ 1,540.5	\$ 1,571.5	\$ 1,757.0	\$ 1,789.8	\$ 1,672.0	2.1%
Assumptions:						
Revenues (2), (4)	\$ 3,361.0	\$ 3,580.9	\$ 3,270.8	\$ 3,112.4	\$ 3,159.3	-1.5%
Personal Income	\$ 41,893.5	\$ 43,455.0	\$ 43,635.3	\$ 43,854.8	\$ 45,291.8	2.0%
Population (5)	1,053,136	1,050,788	1,050,788	1,052,567	1,052,886	0.0%

CAGR = Compound Annual Growth Rate
Source: FY 13 Capital Budget

- (1) As of February 1, 2010, all bonds of the Authority were paid in full.
- (2) FY 08 - FY 12 Capital Budgets.
- (3) Based on Net Tax-Supported Debt which includes agency payments.
- (4) Revenues include actual general revenues plus dedicated gas tax transfers.
- (5) Population estimates for 2011 are from the U.S. Census Bureau, September 22, 2011.

As the result of an increase in General Obligation debt and Economic Development Corporation debt, total Net Tax-Supported Debt increased by a CAGR of 2.1% from FY07 to FY11. These increases were partially offset by a 31.1% CAGR decrease in R.I.H.M.F.C. Neighborhood Opportunities Housing Program debt. State personal income grew at an annual compound rate of 2.0% while revenues declined by 1.5% over the same period.

The Governor, with approval by the General Assembly, also authorizes certain departments to finance the acquisition of equipment and the acquisition and improvement of buildings by using capital leases. Capital leases have been used to finance various projects such as the Attorney General's office, the ACI Intake Center, the office complex at Howard Center for the Department of Labor and Training and power generation facilities at the State Colleges and Universities. These capital leases are considered Tax-Supported Debt by bond credit analysts.

The Economic Development Corporation (the "EDC") issues debt that will be paid from State taxes and revenues which represents 13.5% of Net Tax-Supported Debt. This debt contains unusual credit features, which obligate the State to pay debt service under certain expected circumstances. Two such issues (Fidelity and Fleet leases) carry a moral obligation pledge, which requires the State to appropriate funds in the event that certain job hiring targets are met. In the event performance targets are not met, the State is not obligated to pay under the agreements. The purpose of this type of performance-based credit structure is to foster economic development, and to justify such appropriations by the generation of incremental income tax receipts. For this reason, issuance must be carefully monitored and measured for budget purposes.

Projected Tax-Supported Debt: FY12 to FY16

Using figures provided by the State Budget Office, an estimate of the Tax-Supported Debt for the FY12 - FY16 period has been developed along with a forecast of certain debt ratios.

Table 3-3							
Tax-Supported Debt: Fiscal Years 2012 - 2016							
(dollars in millions, principal amount)							
Fiscal Years	2012	2013	2014	2015	2016		CAGR FY 12 - 16
General Obligation Bonds	\$ 1,119.4	\$ 1,187.4	\$ 1,171.4	\$ 1,134.3	\$ 1,103.8		-0.4%
Capital Leases	267.5	254.0	229.7	205.8	176.8		-9.8%
Convention Center Authority	250.5	240.9	230.9	220.3	209.2		-4.4%
Economic Development Corp.	259.3	236.1	251.8	257.9	299.1		3.6%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	-	-	-	-	-		-
Gross Tax-Supported Debt	\$ 1,896.7	\$ 1,918.4	\$ 1,883.8	\$ 1,818.3	\$ 1,788.9		-1.5%
Agency Payments	(22.8)	(21.3)	(19.8)	(18.2)	(16.5)		-7.8%
Net Tax-Supported Debt	\$ 1,873.9	\$ 1,897.1	\$ 1,864.0	\$ 1,800.1	\$ 1,772.4		-1.4%
Annual Net Tax-Supported Debt Service (1)	\$ 217.7	\$ 235.5	\$ 237.6	\$ 256.4	\$ 261.0		4.6%
Debt Ratios: (2)							
Annual Debt Service / Revenues (7.5%)	6.5%	6.7%	6.6%	7.0%	7.1%		2.0%
Net Debt / Personal Income (5% - 6%)	4.0%	3.9%	3.7%	3.4%	3.2%		-5.6%
Net Debt / Capita	\$ 1,779.8	\$ 1,801.8	\$ 1,770.4	\$ 1,709.7	\$ 1,683.4		-1.4%
Assumptions:							
Revenues	\$ 3,338.7	\$ 3,503.0	\$ 3,599.7	\$ 3,652.6	\$ 3,696.3		2.6%
Personal Income	\$ 46,539.9	\$ 48,467.1	\$ 50,460.0	\$ 52,923.2	\$ 55,377.1		4.4%
Population (3)	1,052,886	1,052,886	1,052,886	1,052,886	1,052,886		0.0%
CAGR = Compound Annual Growth Rate							
Source: FY 13 Capital Budget							
(1) Projected Net Tax-Supported Debt Service. FY 13 Capital Budget, page B-14.							
(2) Based on Net Tax-Supported Debt which includes agency payments.							
(3) Population estimates are from the U.S. Census Bureau, September 22, 2011.							

Gross Tax-Supported Debt (excludes adjustments for agency payments) is projected to decrease from \$1,896.7 million in FY12 to \$1,788.9 million in FY16.

State Supported Revenue Debt

State Supported Revenue Debt is payable from specified revenues pledged for debt service which are not general taxes and revenues of the State. The State provides additional credit support to repay this debt only if the pledged revenues are insufficient to meet scheduled debt service payments.

The State provides credit support in a variety of forms. For purposes of this report, State Credit Support is broadly defined to include a contingent commitment to make annual appropriations under a lease, a contingent commitment to seek appropriations to replenish a special debt reserve, direct guarantees of debt payments, commitments to pay all or a portion of debt service under certain conditions, and commitments to provide other payments which indirectly secure or directly pay debt service.

A contingent commitment to seek appropriations to replenish a special debt reserve is known as a “moral obligation” and has special meaning to credit analysts. State laws that authorize moral obligation debt require notification by the Governor to the General Assembly when a deficiency in a special debt service reserve has occurred. The Governor then is required to request an appropriation to replenish the reserve to its required level. Credit analysts view “moral obligation” bonds as a contingent state obligation even though the legislative body is not contractually required to make the requested appropriation.

State Supported Revenue Debt represents a substantial contingent obligation of the State of \$282.7 million at June 30, 2011, down from \$314.0 million at June 30, 2010. While this type of debt is intended to be paid from dedicated revenues generated from financed projects, the State has provided credit support to additionally secure this debt. Because of the implied financial commitment of State support in the event of any unanticipated revenue shortfall, the level of this debt is an important consideration for the credit ratings of the State’s Tax-Supported Debt. Table 3-4 presents the amounts and types of State Supported Revenue Debt for the five years ending June 30, 2011.

Table 3-4						
State Supported Revenue Debt: Fiscal Years 2007 - 2011						
(dollars in millions, principal amount)						
Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
EDC - Providence Place Mall	33.7	32.1	30.4	28.6	26.7	-5.7%
R.I. Housing	292.5	321.8	285.3	267.3	235.2	-5.3%
Industrial Recreational Building Authority - Insured Industrial Facilities Corporation	13.2	10.9	14.1	18.1	20.8	12.0%
Total	\$ 339.4	\$ 364.8	\$ 329.8	\$ 314.0	\$ 282.7	-4.5%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

The largest component of State Supported Revenue Debt is the moral obligation debt of Rhode Island Housing, which has decreased by 57.3 million (CAGR of 5.3%) since 2007. State Supported Revenue Debt decreased by an annual compound rate of 4.5% for the period from FY07 to FY11.

The Rhode Island Industrial Facilities Corporation (“RIIFC”) issues bonds which are secured by loans and mortgages of private borrowers, but the bonds may be additionally secured by a voter authorized commitment provided by the Industrial-Recreational Building Authority (“IRBA”) which is funded by State appropriations. The portion of RIIFC’s debt guaranteed by IRBA is shown in this category.

The EDC is authorized to secure certain of its revenue bonds with the State moral obligation with the approval of the Governor and as of FY00, all debt issues previously secured under the traditional moral obligation pledge had been paid off. However, there were additional issues authorized by the General Assembly secured by the State’s Moral Obligation, including \$75 million Job Guaranty Program Revenue Bonds issued in FY11 and an additional 5.5 million were issued in FY12.

Agency Revenue Debt

Agency Revenue Debt is similar to the previous classification, except that the State has not provided any form of credit support and no general taxes or revenues are pledged for payment of these bonds. This type of debt is isolated from the State’s general credit, but because the borrowers are agencies or corporations created by the General Assembly, this debt is not as removed as Conduit Debt.

Investors would expect that the State would take no actions which would cause these bond issuers financial harm, and the State has no legal responsibility to prevent financial defaults. However, as a practical matter, the State facilities which are financed in this manner, such as the University of Rhode Island, the Claiborne Pell and Mt. Hope Bridges, and the T.F. Green Airport expansion, are important public facilities, the use of which the State would not likely surrender in the event that the pledged revenues were insufficient to pay debt service. For this reason, this type of debt is important to the State’s credit standing.

The State has issued general obligation bonds to finance facilities of several of the agencies shown in Table 3-5. Only the Revenue Debt of these agencies is presented in Table 3-5, and any other debt is presented in the sections relating to Tax-Supported Debt. Table 3-5 presents the amounts and types of Agency Revenue Debt for five fiscal years ending June 30, 2011.

Table 3-5						
Agency Revenue Debt: Fiscal Years 2007 - 2011						
(dollars in millions, principal amount)						
Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
Airport Corporation	\$ 308.0	\$ 334.8	\$ 327.7	\$ 319.7	\$ 309.7	0.1%
Economic Development Corporation	67.8	77.2	94.4	94.0	97.5	9.5%
EDC - GARVEE Bonds, Federally Funded	207.8	285.5	427.4	400.5	372.3	15.7%
R.I. Housing	5.0	5.0	5.0	5.0	5.0	0.0%
Narragansett Bay Commission	444.7	463.2	444.0	410.1	422.4	-1.3%
Resource Recovery Corporation	16.2	14.5	14.8	14.0	13.1	-5.2%
State University and Colleges	199.3	195.1	222.6	283.1	276.2	8.5%
Turnpike and Bridge Authority	27.8	25.7	23.6	70.7	69.2	25.6%
Water Resources Board	8.3	7.5	5.8	4.9	4.1	-16.2%
Total	\$ 1,284.9	\$ 1,408.5	\$ 1,565.3	\$ 1,602.0	\$ 1,569.5	5.1%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

The Turnpike and Bridge Authority experienced the largest increase of 25.6% followed by the EDC – GARVEE Bonds at 15.7%. Next was the Economic Development Corporation which increased by 9.5% and the State University and Colleges which increased by 8.5% because of various construction and improvement projects. Overall, Agency Revenue debt grew at a compound annual rate of 5.1% from FY07 - FY11. Because payment of this category of debt is supported by fees, charges, or other revenues, an increase in this type of debt may be considered as one indicator of economic growth. However, either a stable or growing economy is needed to support such debt.

Conduit Debt

Conduit Debt is issued by a state agency on behalf of borrowers, which include businesses, health care institutions, private higher education institutions, local governments, and qualified individuals (loans for housing and higher education purposes). These borrowers are able to borrow at the favorable tax exempt interest rates under the federal tax laws by having a State agency issue bonds on their behalf.

Conduit Bonds are payable from repayment of loans by the borrowers and are independent of the State’s credit. Investors would not expect any assistance by the State in the event the borrower experienced financial difficulties or if the debt were to default. None of the debt presented in Table 3-6 is secured by any form of State Credit Support.

Table 3-6						
Conduit Debt: Fiscal Years 2007 - 2011						
(dollars in millions, principal amount)						
Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11
Clean Water Finance Agency	\$ 576.9	\$ 631.3	\$ 602.6	\$ 652.7	\$ 671.2	3.9%
Health and Educational Building Corporation	1,908.0	2,225.4	2,377.6	1,793.7	2,574.5	7.8%
R.I. Housing	1,234.5	1,289.6	1,293.7	1,445.1	1,416.5	3.5%
Industrial Facilities Corporation	105.2	86.1	89.3	95.3	80.8	-6.4%
Student Loan Authority	889.6	946.8	1,046.3	1,331.4	1,026.6	3.6%
Water Resources Board	3.0	2.0	1.0	-	-	-100.0%
Total	\$ 4,717.2	\$ 5,181.2	\$ 5,410.5	\$ 5,318.2	\$ 5,769.6	5.2%
CAGR = Compound Annual Growth Rate						
Source: Treasury Survey of R.I. Quasi-Public Corporations.						

Conduit Debt, which represents the largest category of debt, grew at a compound annual rate of 5.2% from FY07 - FY11. The agencies which experienced the most significant growth in debt were the Health and Educational Building Corporation and the Clean Water Finance Agency with compound annual growth rates of 7.8% and 3.9% respectively. The Student Loan Authority and R.I. Housing debt levels have also been on the rise, but at a slower rate.

Local Government Debt

Local governments issue various types of debt which may be secured by a general obligation of the local government or may be payable from a specific revenue source.

Table 3-7 presents the amounts of Local Government Debt for the five years ending June 30, 2011. This table does not include the debt of certain regional and municipal authorities including the Bristol County Water Authority, the Foster Gloucester Regional School District, Kent County Water Authority, and the Providence Public Building Authority.

Table 3-7							
Local Government Debt: Fiscal Years 2007 - 2011							
(in millions)							
Fiscal Years	2007	2008	2009	2010	2011	CAGR FY 07 - 11	
Local Government Debt	\$ 1,498.5	\$ 1,713.7	\$ 1,692.0	\$ 1,767.6	\$ 1,821.3	5.0%	
CAGR = Compound Annual Growth Rate							
Source: Office of the General Treasurer and the Audited Financial Statements of the 39 Cities and Towns.							

Local government debt includes general obligation bonds and notes, revenue bonds, and capital leases of Rhode Island’s 39 local governments. During the five years shown in Table 3-7 this debt grew at a compound annual growth rate of 5.0%.

SECTION 4

Debt Policies and Practices

Importance of Debt Management

The State of Rhode Island and its local governments use debt to finance capital improvements and to make loans at tax exempt interest rates to various government, nonprofit, and private borrowers for capital investments for economic development and other public purposes. The ability to fund capital investments through borrowing is important because the State and its local governments do not have sufficient cash reserves or dedicated revenue resources necessary to fund these expenditures. Of course, not all capital investments are funded or should be funded with debt. Current revenues and cash reserves also are and should remain as funding sources for capital improvements for the State and its local governments.

Maintaining an ability to borrow, often called “debt capacity,” is a critical resource for most state and local governments. Without debt capacity the State may not be able to pay for restoration of aging infrastructure and make new capital investment. Public capital investment attracts private capital to be invested, which creates employment and a high quality of life for the citizens of the State. Capital investment in transportation infrastructure, including highways, airports, and ports, is a basic building block for the State’s economy. Other essential capital investments must be continually made for purposes such as water, wastewater, recreation, local schools, and higher education. The State’s capital budget lays out future State capital needs. Because of the State’s current debt profile, prudent debt management is critical to satisfying these capital investment needs.

Debt Limits and Targets

Setting debt targets is a policy exercise involving balancing the cost of debt against the need for debt financed capital improvements. Many states set limits on debt that is paid from state general taxes and revenues. Maintaining a high credit rating or improving an average rating is a key objective in limiting debt in most states. The PFMB has set debt limits based on personal income levels and debt service as a percentage of General Revenues. However, municipal/public credit ratings are based on not only debt levels, but also financial, economic and management characteristics of the jurisdiction. There are no fixed formulas for the optimal combination of these factors. In reality, some factors, such as the economy or demographics, are beyond the issuer’s control. However, because debt issuance can be controlled, most borrowers focus on debt levels as a critical rating factor. The principal benefit of higher credit ratings is that investors are willing to accept lower interest rates on highly rated debt relative to lower rated debt; thereby reducing the State’s borrowing costs.

Debt Capacity

For purposes of this analysis, debt capacity is a term used to define how much debt can be issued by the State or an agency of the State, either on an absolute basis or without adverse consequences to its credit rating or the marketability of its debt. Debt capacity is customarily evaluated in view of the income, wealth, or asset base by which the debt is secured or from which it is paid. With the variety of debt types, payment sources and legal means used to secure debt, there is no single measure of debt capacity to which all debt issued by all state agencies would be subject.

Rhode Island made presentations to the State’s credit rating agencies on several occasions in 2010 and 2011. The agencies were provided with an update of the State’s budget, economic development initiatives and current debt profile. The ratings were based on the State’s economic performance, effective management of the State’s financial operations, and success in reducing the State’s debt burden, economic development efforts and recent

pension reform. Post recalibration, Rhode Island's general obligation bonds are currently rated "Aa2/AA/AA" by Moody's Investors Service, Standard & Poor's and Fitch, respectively. It is important to note that the State maintained its ratings level during the period 2001-2004, when many states were downgraded or placed on credit watch. However, in November 2007 when the State again met with all three rating agencies, their focus was on the State's budget situation. While all three rating agencies rate Rhode Island in the "Double A" category, recent rating reports include warning signs. One rating agency noted the State's use of one-time tobacco revenues to balance the 2007 and 2008 budgets which evidenced "continuing financial strain at a time when most states are moving toward structurally balanced budgets." It is clear that the rating agencies will continue to scrutinize the budget process carefully. There is no doubt that the projected budget deficit and actions taken to continue to address the projected deficit will be an important rating consideration. The State's financial and budgeting practices and track record in reducing the debt burden and taking appropriate action in response to budget pressures have been recognized as credit strengths in the past. Challenges to the State's ratings are presented by the projected budget deficits in the out year forecast, a relatively weaker economy and declining revenues combined with budgetary pressure for human services, infrastructure needs and the ability to maintain adequate reserves. The State's response to these challenges will be closely monitored by the rating agencies. No longer can the State rely on one-time revenues to balance its budget. Table 4-1 presents the credit ratings for all states with general obligation debt outstanding.

Debt projections for FY12 through FY16, as presented in Table 3-3, indicate that Debt to Personal Income will decrease from 4.0% to 3.2% during this period. These projections also show Debt Per Capita decreasing by 1.4% from \$1,779.8 to \$1,683.4 over the same period.

Because the rating agencies also evaluate economic and demographic factors in their rating analyses, the State's economic and demographic growth relative to other states will be a key factor in future comparisons. Finally, while the State's Debt to Personal Income of 4.7% in FY11 compares favorably to Moody's 2011 peer group average of 5.2%, this ratio is high relative to Moody's 2011 median (includes all states) of 2.8%. Likewise, the State's FY11 Debt per Capita of \$1,997 compares unfavorably to the current Moody's median at \$1,117, but favorably to the 2011 Peer Group Average of \$2,500. Debt levels tend to be relatively higher in Rhode Island's Peer Group states in light of their aging infrastructure and practice of financing projects at the state level rather than at the municipal or county level. These comparisons indicate that even after projected debt ratio improvements, Rhode Island's debt profile will continue to remain high relative to other states. These projections support Rhode Island's continued discipline in debt management.

**Table 4-1
Long Term Credit Ratings
General Obligation Bonds**

	<u>Moody's</u>	<u>S & P</u>	<u>Fitch</u>
Alabama	Aa1	AA	AA+
Alaska	Aaa	AAA	AA+
Arizona	Aa3	AA-	NR
Arkansas	Aa1	AA	NR
California	A1	A-	A-
Colorado	Aa1	AA	NR
Connecticut	Aa3	AA	AA
Delaware	Aaa	AAA	AAA
Florida	Aa1	AAA	AAA
Georgia	Aaa	AAA	AAA
Hawaii	Aa2	AA	AA
Idaho	Aa1	AA+	AA
Illinois	A2	A+	A
Indiana	Aaa	AAA	AA+
Iowa	Aaa	AAA	AAA
Kansas	Aa1	AA+	AA
Kentucky	Aa2	AA-	AA-
Louisiana	Aa2	AA	AA
Maine	Aa2	AA	AA+
Maryland	Aaa	AAA	AAA
Massachusetts	Aa1	AA+	AA+
Michigan	Aa2	AA-	AA-
Minnesota	Aa1	AA+	AA+
Mississippi	Aa2	AA	AA+
Missouri	Aaa	AAA	AAA
Montana	Aa1	AA	AA+
Nebraska	Aa2	AAA	NR
Nevada	Aa2	AA	AA+
New Hampshire	Aa1	AA	AA+
New Jersey	Aa3	AA-	AA-
New Mexico	Aaa	AA+	NR
New York	Aa2	AA	AA
North Carolina	Aaa	AAA	AAA
North Dakota	Aa1	AA+	NR
Ohio	Aa1	AA+	AA+
Oklahoma	Aa2	AA+	AA+
Oregon	Aa1	AA+	AA+
Pennsylvania	Aa1	AA	AA+
Rhode Island	Aa2	AA	AA
South Carolina	Aaa	AA+	AAA
South Dakota	Aa2	AA+	AA
Tennessee	Aaa	AA+	AAA
Texas	Aaa	AA+	AAA
Utah	Aaa	AAA	AAA
Vermont	Aaa	AA+	AAA
Virginia	Aaa	AAA	AAA
Washington	Aa1	AA+	AA+
West Virginia	Aa1	AA	AA+
Wisconsin	Aa2	AA	AA
Wyoming	NR	AAA	NR
Rhode Island rating compared to other states:			
Above Rhode Island	31	28	29
Same as Rhode Island	12	15	8
Below Rhode Island	5	6	5
NR	1	0	7
Source: First Southwest Company - State Ratings as of 5/29/12.			

Tax-Supported Debt

Tables 4-2, 4-3, and 4-4 present the history for the key debt ratios for Rhode Island and the median level for all states as determined periodically by Moody's Investors Service. The peer states of Delaware, Connecticut, Massachusetts, Maine, New Hampshire, and Vermont were selected due to geographical proximity (the New England states), population (Delaware, Vermont, New Hampshire, Maine), age of infrastructure (all), and concentration of services at the state level (Delaware).

		RI								
		National	Moody's	Peer						
Year	RI	Rank	Median	State Ave	DE	CT	MA	ME	NH	VT
2001	5.3%	7th	2.1%	4.8%	5.5%	8.0%	8.5%	2.0%	1.5%	3.3%
2002	5.2%	7th	2.3%	4.7%	5.3%	8.0%	8.5%	1.9%	1.5%	3.0%
2003	5.0%	7th	2.2%	4.7%	5.0%	8.2%	8.5%	1.8%	1.4%	3.0%
2004	4.4%	12th	2.4%	4.7%	5.6%	8.4%	8.5%	1.8%	1.5%	2.5%
2005	4.3%	16th	2.4%	4.7%	5.5%	8.5%	8.5%	2.2%	1.3%	2.3%
2006	4.1%	13th	2.5%	4.8%	5.3%	8.0%	9.8%	2.0%	1.4%	2.2%
2007	4.6%	13th	2.4%	4.7%	5.5%	7.8%	9.4%	1.9%	1.3%	2.1%
2008	4.7%	12th	2.6%	4.6%	5.2%	7.3%	9.8%	1.9%	1.3%	2.0%
2009	4.5%	11th	2.5%	4.6%	5.4%	8.2%	8.9%	2.2%	1.3%	1.8%
2010	5.2%	13th	2.5%	5.0%	6.2%	8.7%	9.2%	2.2%	1.6%	1.8%
2011	4.7%	14th	2.8%	5.2%	6.8%	9.1%	9.4%	2.3%	1.8%	2.0%
Source:	Moody's Investors Service									
	May 22, 2012 - State Debt Medians Report									

Note: Due to variations in calculation methods used by Moody's, Rhode Island's debt ratios in this table are different than the same ratios which are presented in Table 3-2.

The Tax-Supported Debt to personal income ratio measures the State's debt paid from general taxes and revenues in comparison to personal income, which is considered to be a good measure of the State's aggregate wealth. Rhode Island's Net Tax-Supported Debt to Personal Income ratio had decreased every year from 2001 - 2006 and its ranking dropped from the 7th highest in the country to the 13th highest. The 2005 ratio of 4.3% improved due to Tobacco Securitization and was below the peer group average of 4.7%, but it still remains well above Moody's median of 2.4%. However, in 2011 the ratio increased to 4.7% giving Rhode Island a ranking of 14th highest. This indicates that Rhode Island's Tax-Supported Debt is a greater burden on the State's economy than is typical of most states. Personal income represents the wealth of the State which is taxed to support Tax-Supported Debt or could be taxed to support State Credit Supported Revenue Debt.

**Table 4-3
Comparison to Peer States
Net Tax-Supported Debt per Capita**

<u>Year</u>	<u>RI</u>	<u>RI National Rank</u>	<u>Moody's Median</u>	<u>Peer State Ave</u>	<u>DE</u>	<u>CT</u>	<u>MA</u>	<u>ME</u>	<u>NH</u>	<u>VT</u>
2001	\$ 1,497	7th	\$ 541	\$ 1,565	\$ 1,616	\$ 3,037	\$ 2,957	\$ 487	\$ 463	\$ 828
2002	\$ 1,552	7th	\$ 573	\$ 1,660	\$ 1,650	\$ 3,240	\$ 3,267	\$ 485	\$ 503	\$ 813
2003	\$ 1,508	7th	\$ 606	\$ 1,692	\$ 1,599	\$ 3,440	\$ 3,298	\$ 471	\$ 485	\$ 861
2004	\$ 1,385	9th	\$ 701	\$ 1,734	\$ 1,800	\$ 3,558	\$ 3,333	\$ 492	\$ 496	\$ 724
2005	\$ 1,402	11th	\$ 754	\$ 1,904	\$ 1,845	\$ 3,624	\$ 4,128	\$ 606	\$ 514	\$ 707
2006	\$ 1,687	9th	\$ 787	\$ 1,944	\$ 1,998	\$ 3,713	\$ 4,153	\$ 603	\$ 492	\$ 706
2007	\$ 1,766	9th	\$ 889	\$ 2,009	\$ 2,002	\$ 3,698	\$ 4,529	\$ 618	\$ 499	\$ 707
2008	\$ 1,812	9th	\$ 865	\$ 2,150	\$ 2,128	\$ 4,490	\$ 4,323	\$ 743	\$ 525	\$ 692
2009	\$ 2,127	9th	\$ 936	\$ 2,348	\$ 2,489	\$ 4,859	\$ 4,606	\$ 760	\$ 665	\$ 709
2010	\$ 2,191	10th	\$ 1,066	\$ 2,508	\$ 2,676	\$ 5,236	\$ 4,711	\$ 865	\$ 812	\$ 747
2011	\$ 1,997	12th	\$ 1,117	\$ 2,500	\$ 2,674	\$ 5,096	\$ 4,814	\$ 845	\$ 776	\$ 792

Source: Moody's Investors Service
May 22, 2012 - State Debt Medians Report

Note: Due to variations in calculation methods used by Moody's, Rhode Island's debt ratios in this table are different than the same ratios which are presented in Table 3-2.

The ratio of Tax-Supported Debt to population fails to consider the economic wealth that supports the debt or the portion of the State's budget used to pay debt service. This ratio shows that three of the six peer states (Delaware, Connecticut and Massachusetts), have levels of debt per capita above the national median. This may be due to the combined factors of age of infrastructure, low population, and the dependency on the state to shoulder greater financing responsibilities. Since 2001, Rhode Island's Net Tax-Supported Debt per Capita has consistently been below that of the peer state average.

**Table 4-4
Tax-Supported Debt Service as a Percent of General Revenues**

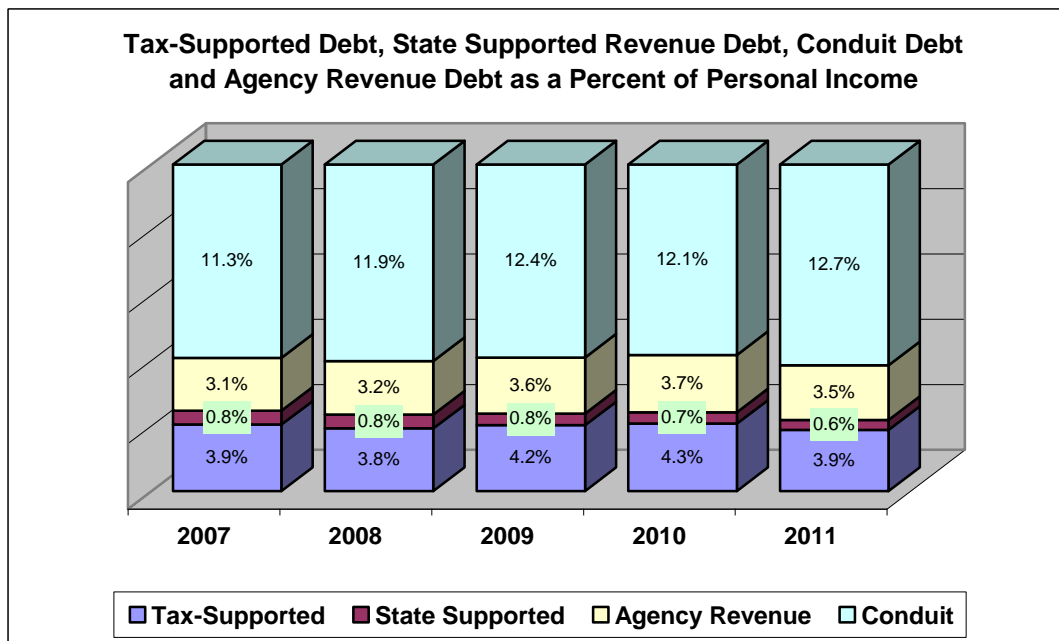
<u>Year</u>	<u>RI</u>
2007	5.2%
2008	5.2%
2009	6.0%
2010	7.0%
2011	6.7%

Source: FY 08 - FY 12 Capital Budgets.

Tax-Supported Debt Service to General Revenues is used for internal trend analysis, but no longer for peer group comparison analysis since the rating agencies no longer publish this data.

As Tables 4-2 and 4-3 show, Rhode Island has moderately high levels of Tax-Supported Debt according to these ratio measures. It should be noted, however, that tax supported debt as a per cent of personal income has declined somewhat since 2009 as shown in the chart below. High debt levels can lead to lower credit ratings, which result in higher borrowing costs, and a diminished financial capacity to respond to needed infrastructure improvements to support economic development.

As shown in the chart below, the total amount of Rhode Island’s Tax-Supported Debt, State Supported Revenue Debt, Agency Revenue Debt and Conduit Debt and its relationship to State personal income has increased from 19.0% of Personal Income in FY07 to 20.7% in FY11. This increase came as Personal Income grew at the compound annual growth rate of 2.0%.



Section 5

Recommended Priorities and Issues for 2012 and 2013

Based on the findings of this and the preceding Debt Management Reports, the following debt management priorities are recommended for 2012 and 2013.

1. Institutionalize and continue to improve Disclosure Practices

Improved Disclosure has been one of the General Treasurer's top priorities. During FY 2011, the State retained Special Disclosure Counsel and reconstituted its Disclosure Working Group. Regular training for Staff will be in place by the end of FY 2011. Training was expanded to include state agencies during FY 2012 and will be offered to municipalities in FY 2013. The Municipal Markets place increasing importance on Issuer Disclosure Information, not only when bonds are issued, but on a continuing basis. The State will consider the white papers being developed by the National Federation of Municipal Analyst and the National Association of Bond Lawyers in improving Disclosure Practices. In addition to offering training, the State will offer to extend Disclosure expertise to municipalities and other issuers in Rhode Island.

2. Enhanced Investor Relations Program

It is recommended that the State continue to improve its Investor Relations program to enhance the participation of Rhode Island "retail" investors in the purchase of State issued debt and to respond to the information needs of institutional investors. This effort will also serve to provide appropriate information to the marketplace on an ongoing basis. This initiative requires the assistance of the State's Bond Counsel, Disclosure Counsel, Special Disclosure Counsel and Financial Advisor. Market developments over the past few years have made analysis of the issuer's underlying credit more important to the investment decision. Therefore, improved Disclosure and Investor Relations can enhance an issuer's place in the market. As a first step, the Treasurer's office upgraded its website and added an investor relations portal. In addition, investor road shows, both in person and web-based have been undertaken, as well as direct outreach to major institutional investors.

3. Continued Emphasis on Rating Agency Communication and Debt Management

Rhode Island's improved debt position relative to the 50 states over the past decade is the product of policies and fiscal discipline adopted after the State's debt burden peaked in the early '90s. Rhode Island's relative position nationally improved from 7th highest ratio of debt to personal income in 2001 to 14th highest in 2011. The State's debt management policies included greater scrutiny of debt issues, the development of debt level benchmarks and refinement of the capital budgeting process. Rhode Island has lived up to its commitment to reduce its debt burden and is now realizing the benefits of this consistent discipline. Recent changes in rating agency criteria have incorporated Pension and OPEB liabilities in the analysis of overall debt burden. Rhode Island's past efforts related to retiree health care and its pension systems have been a positive development. However, more progress needs to be made in this area to manage future liabilities.

The credit guidelines and more conservative debt ratio targets approved by the PFMB in June 2000 provided the structure necessary to evaluate debt trends for the past 12 years. It is also appropriate, however, to review those guidelines in the context of new rating agency criteria and economic conditions and going forward, to look broadly at the debt approval process of the State and quasi-public agencies for opportunities to improve the review process and to strengthen controls.

Maintenance of the State's AA category ratings is more important now than ever before, as credit spreads are at their widest levels in decades and credit enhancement is only thinly available. Challenges to the State's ratings include a weak economy and declining revenues, budgetary pressure for human services, infrastructure needs, and the ability to maintain adequate reserves. The State's responses to these challenges will be closely monitored by the rating agencies. During periods such as these, regular communication with the rating analysts is critical and the State will continue to meet with the rating agencies on a regular basis and not solely in connection with the issuance of debt.

4. Sponsor Educational Programs for Municipalities

The PFMB can provide a much-needed service in offering continuing education on topical issues to municipal officers. Initiatives in this area have continued. In 2012, the Office of the General Treasurer hosted meetings and seminars for municipalities on pension reform and investments. In January 2011, the Office of the General Treasurer participated in a panel discussion for municipal officials at the Rhode Island League of Cities and Towns annual trade show on OPEB liabilities and funding. In February 2010, the Office participated in a RI League panel discussion for municipal officials on ARRA related financing opportunities. In October 2008, the Office of the General Treasurer hosted a seminar for Municipal and State officials. In the past, staff from the Office of General Treasurer worked with municipal finance officers and the Rhode Island Public Expenditure Council ("RIPEC") to develop a "Municipal Fiscal Healthcheck" to provide uniform data on the fiscal practices, policies, and status of all municipalities. The Office of the General Treasurer also supports the efforts of the Rhode Island Government Finance Officers Association ("RIGFOA") and has been involved in reviewing legislation to improve local borrowing practices, making presentations at RIGFOA meetings and the development of programs for RIGFOA members. In past years, topics included the State Retirement System, Cash Management and Other Post Employment Benefits. Future topics will include Performance Measures and Benchmarks, Disclosure Practices and Pension and OPEB Reform.

5. Explore Alternative Funding Mechanisms for Major Transportation and Infrastructure Projects

The State's Capital Budget and Transportation Improvement Plan ("TIP") have included significant increases in capital spending for major infrastructure projects such as the relocation of Route I-195. Revenues from the gasoline tax provide support for Transportation projects and the State General Fund. That revenue source has not kept pace with DOT's budget with debt service on General Obligation Bonds sold to prove the State match for Federal Highway funds requiring an increasing portion of the allocation. Dedication of additional revenues to Transportation will reduce the State's reliance on debt to provide State match and foster the stated PFMB and State goals of reducing or moderating Rhode Island's reliance on tax-supported debt for such projects. The PFMB should also monitor the work of Treasury staff and the State Administration to explore innovative funding mechanisms for major infrastructure projects. For example, Treasury staff reviewed the Garvee and Motor Fuel Tax bond issue structures as part of the November 2003, March 2006 and April 2009 issues. The State's efforts to wean the DOT from borrowing for State match for Federal Highway funds through the allocation of certain fees and RICAP funds to that purpose is a credit positive.

Several states explored public private partnerships or privatization of certain government assets to finance and/or manage certain projects such as roads and bridges. While private management can be a benefit with appropriate oversight, leveraging government assets often results in the loss of control over the project as well as user fees and costs to constituents. Recent trends in the credit markets increased the cost differential between

conventional financing and private financing. All such factors must be considered prior to moving forward with such an initiative.

6. Responding to Changes in the Municipal Bond Market and Regulatory Environment

The global credit crisis of 2008 had a major impact on the municipal bond market. The ability to access the capital markets has become increasingly challenging for issuers such as the State. The demise of the municipal bond insurance industry coupled with the credit squeeze and the notable absence of several major investment banking firms will have an impact on the State as it seeks to finance its capital needs. The State successfully sold its Tax Anticipation Notes for FY 2009 and 2010 and Certificates of Participation for new projects during the past year. Navigating these elements will continue to be a significant priority for the State to insure continued access to capital at affordable levels.

The Dodd-Frank Wall Street Reform and Consumer Protection Act includes many provisions that will have an impact on the municipal market including banking provisions and regulation and registration of municipal finance advisors. The Municipal Securities Rulemaking Board has new powers relating to issuers and advisors and the State will need to monitor these developments closely.

7. Monitor subsidies relating to American Recovery and Reinvestment Act of 2009 programs

The American Recovery and Reinvestment Act (ARRA) of 2009 included several municipal bond provisions that can benefit the State and its agencies and municipalities. The Office of the General Treasurer was involved in evaluating the applicability of Build America Bonds, Recovery Zone Bonds and Qualified School Construction Bonds. In 2010, the State acted quickly to take advantage of the provisions for Recovery Zone Bonds or “Super BABs” which provided a 45% subsidy off a taxable interest rate. It will be important to monitor the procedures for applying the federal subsidy for each interest payment.

8.

Monitor Moral Obligation Debt More Closely

The EDC Job Guaranty Revenue Bonds funded a loan to a private company. Less than two years after the loan was made, that company filed for bankruptcy. It is the recommendation of the PFMB that the EDC or any other issuer of Moral Obligation Bonds require quarterly financial reports from the borrowers and report annually to the General Assembly on the status of the borrower payments.