Fiscal Year 2009 Report on Debt Management
To the
Public Finance Management Board

November 2010

State of Rhode Island
And Providence Plantations

OFFICE OF THE GENERAL TREASURER

FRANK T. CAPRIO
GENERAL TREASURER

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November 2010

Members of the Rhode Island Public Finance Management Board

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Mr. Robert A. Mancini, Public Member
Mr. Edward F. Yazbak, Public Member
Mr. Emanuel Barrows, Public Member
Mr. Thomas M. Bruce, III Public Member

Dear Members of the Board:

I hereby submit the fiscal year 2009 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 position relative to the State's borrowing capacity as part of Rhode Island's efforts to maintain fiscal discipline.

Rhode Island's debt burden peaked in the 1990's and for years the State was ranked in the top three nationally in terms of debt as a percentage of personal income and debt per capita. 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 1999, Rhode Island's debt burden was the 5th highest nationally according to Moody's Investors Service. The 2009 State Debt Medians Moody's recently published show that Rhode Island's ranking has dropped to 9th for debt per capita and 11th for debt as a percentage of personal income.

Net tax supported debt totaled $1.85 billion at the close of FY 2009 and current Budget Office forecasts project the State's debt level to increase to $1.96 billion by FY 2014.
Efforts to increase pay-as-you-go financing of projects, reactivate the sinking fund to defease high-cost debt or to limit, to the extent possible, issuing new debt, and improve bonds proceeds management must be continued. We are also pleased to report that the integrated debt management system the Office of the General Treasurer, the Budget Office and the Office of Accounts and Control implemented in 2005 has improved debt administration and reporting.

In order to maintain its credit ratings at an appropriate level, the State must continue to make fiscal responsibility a top priority. 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 rating 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.

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

In 2008, the State of Rhode Island was downgraded by one rating agency and has had a negative outlook assigned to its rating by two of the rating agencies. One rating agency noted the State's use of one-time tobacco revenues to balance the 2007 and 2008 budgets evidenced "continuing financial strain at a time when most states are moving toward structurally balanced budgets."

In past years, Rhode Island was favorably cited for its fiscal discipline. Notably, when Standard & Poor's Rating Agency last upgraded the State of Rhode Island from "AA-" to "AA" in November 2005, the rating report credited the State's pension reform measures as one of the positive factors in the upgrade. Financial management processes continue to be rated as "Strong" by Standard & Poor's. Other credit characteristics which supported the rating upgrade at that time included ***consistent financial performance and statutory reserves.*** The rating agency also noted that certain factors offset these strengths, including, a sizable unfunded pension liability. In order to preserve its current rating level, Rhode Island will need to demonstrate structural balance between revenues and expenditures. To that end, I have communicated with the Legislative Leadership to discuss the concerns raised by the rating agencies.

This past spring, two of the municipal rating agencies recalibrated municipal ratings. Fitch completed their process in April and Moody's recalibrated the states in May of 2010. Standard & Poor's has been using one rating scale for the past two years. These actions are 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 are not viewed as improvements in credit quality or rating upgrades, but as an alignment of municipal ratings with corporate or global equivalents.

Recalibration has proven to be important to so called "cross-over" buyers who typically consider investments in taxable securities. The special subsidized and tax credit bond programs authorized under the American Recovery and Reinvestment Act (ARRA) resulted in a dramatic increase in volume of taxable municipal debt.

Much of the rating analysis is based upon economic and related factors. For example, Moody's has had the state government sector on negative outlook since February 2008. This outlook reflects weak revenue performance over three fiscal years. As a whole, states have responded by reducing expenditures, depleting reserves and in some cases increasing revenues to weather the economic downturn. In addition, State budgets have had to rely on ARRA funds to achieve balance in FY 2010 and FY 2011.

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

The State's credit rating agencies will continue to scrutinize 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 have been at their widest levels in decades. 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 equal or exceed the PFMB's guideline of 7.5% beginning in FY12. Projections indicate that the FY12 through FY14 debt service to revenues ratio will reach 7.5%, 7.8% and 7.7% respectively. The economic climate of the past two 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,

SECTION 1
2009 Findings

The 2009 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 Special Comment Report, May 2010 and the FY11 Capital Budget:

- Rhode Island ranks 11th highest among all states in Net Tax Supported Debt as a percent of personal income, at 4.5% (based on Moody's calculations and 2007 personal income).
- Rhode Island ranks 9th highest among all states in Net Tax Supported Debt per capita at $2,127 (based on Moody's calculations).
- Net Tax Supported Debt increased annually by 7.4% from FY05 - FY09. Personal income growth for the same period was 3.4%.
- In FY09 the general obligation debt increased at a rate of 3.9% over FY08. From FY05 - FY09 general obligation debt increased at a rate of 6.7%.

Over the last four years, Net Tax-Supported Debt increased by $456.8 million, from $1.39 billion at FY05 to $1.85 billion at FY09. Current Tax-Supported Debt of $1.85 billion represents an increase of 11.8% from $1.65 billion at FY08. Rhode Island's Tax-Supported Debt peaked at FY94 at $1.88 billion.

According to the FY11 Capital Budget, the State's outstanding Net Tax Supported Debt (includes adjustment for agency payments) is projected to increase to $1.96 billion for FY14. 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 FY11 also indicates that State general obligation debt will increase at a compound annual growth rate of 1.5% from $1,063.2 million at FY10 to $1,129.5 million at FY14. The Economic Development Corporation debt will decrease at a compound annual growth rate of -9.8%. During the same period, it is estimated that capital leases will increase at a compound annual growth rate of 11.9% and Convention Center Authority will decrease by 3.7%.

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. However, a variety of factors contributed to the Fitch Ratings subsequent downgrade of Rhode Island's rating from AA to AA-. Protecting the gains made in debt reduction is critical and important to preserving financial flexibility.

This past spring, two of the municipal rating agencies recalibrated municipal ratings. Fitch completed their process in April and Moody's recalibrated the states in May of 2010. Standard & Poor's has been using one rating scale for the past two years. These actions are 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 are not viewed as improvements in credit quality or rating upgrades, but as an alignment of municipal ratings with corporate or global equivalents.

Recalibration has proven to be important to so called "cross-over" buyers who typically consider investments in taxable securities. The special subsidized and tax credit bond programs authorized under the American Recovery and Reinvestment Act (ARRA) resulted in a dramatic increase in volume of taxable municipal debt.
Much of the rating analysis is based upon economic and related factors. For example, Moody's has had the state government sector on negative outlook since February 2008. This outlook reflects weak revenue performance over three fiscal years. As a whole, states have responded by reducing expenditures, depleting reserves and in some cases increasing revenues to weather the economic downturn. In addition, State budgets have had to rely on ARRA funds to achieve balance in FY 2010 and FY 2011.

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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.

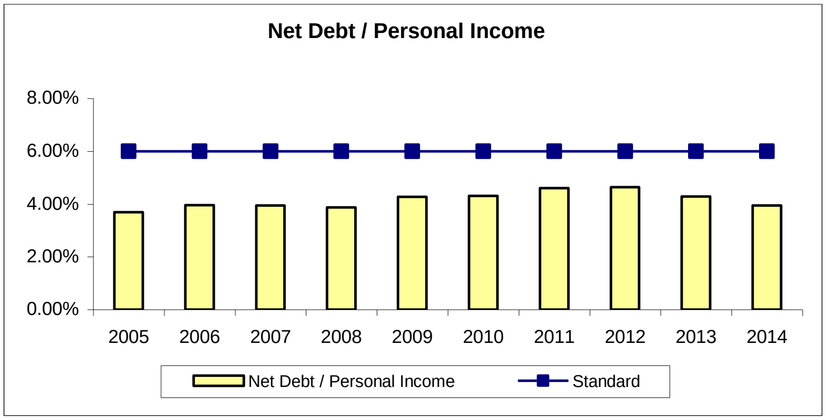
The PFMB approved the following revisions to the Tax Supported Debt to Personal Income target debt ratios recommended in the 1999 Report on Debt Management. Approved guidelines are as follows:

- ***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.

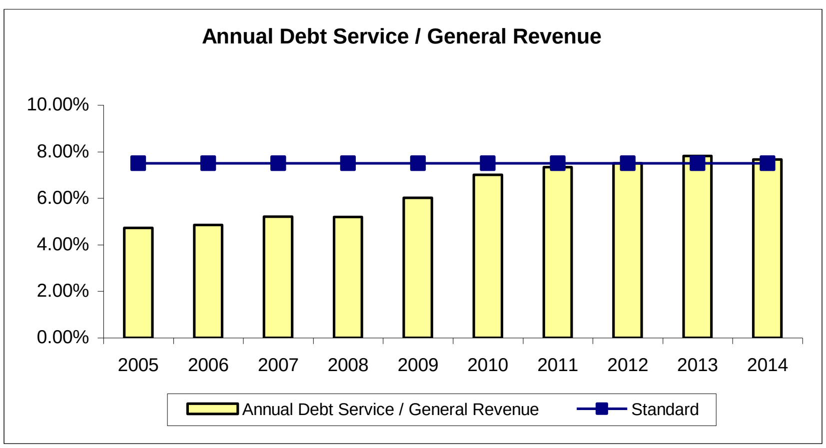
- ***Credit Guideline 2:*** The Board should monitor the total amount of Tax Supported Debt, State Supported Revenue Debt, and Agency Revenue Debt in relation to the State's personal income.

- ***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 will remain within the Credit Guidelines relating to Net Debt to Personal Income, as the ratio will decline from 4.3% at FY10 to 4.0% at FY14. From FY05 to FY09, Personal Income grew at a rate of 3.4%, while Net Tax-Supported Debt increased by 7.4%. The combination of lower Personal Income growth and moderate debt growth resulted in the Net Debt to Personal Income ratio of 3.7% at FY05 increasing to 4.3% for FY09.



Annual Debt Service as a percentage of revenues increased from 4.7% in FY05 to 6.0% in FY09. Projections from FY10 to FY14 indicate a break with the PFMB's guidelines as the FY13 and FY14 debt service to revenues ratio exceeds the 7.5% target at 7.8% and 7.7% respectively.

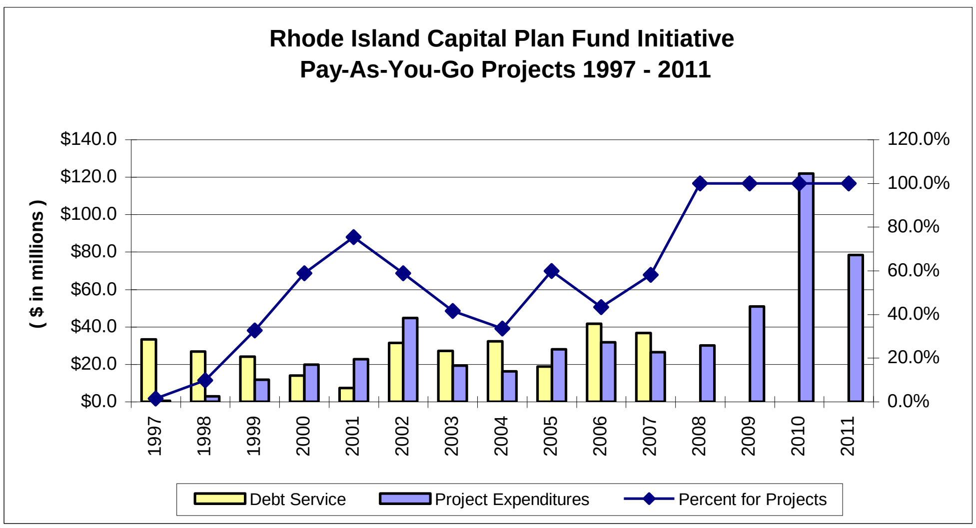


Positive Steps in Debt Administration

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 has 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 2010. Greater financial flexibility during periods of economic expansion have 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.

   Included in the governor's recommended FY11 Budget was a $78.3 million appropriation ($121.9 million in FY10 which includes funding reappropriations from FY09) for pay-as-you-go capital financing through the Rhode Island Capital Plan Fund. Funds may be used to pay for debt service or project expenditures. According to the FY11 Capital Budget, 100.0% of the Fund's resources will be used for capital asset protection projects in FY11.



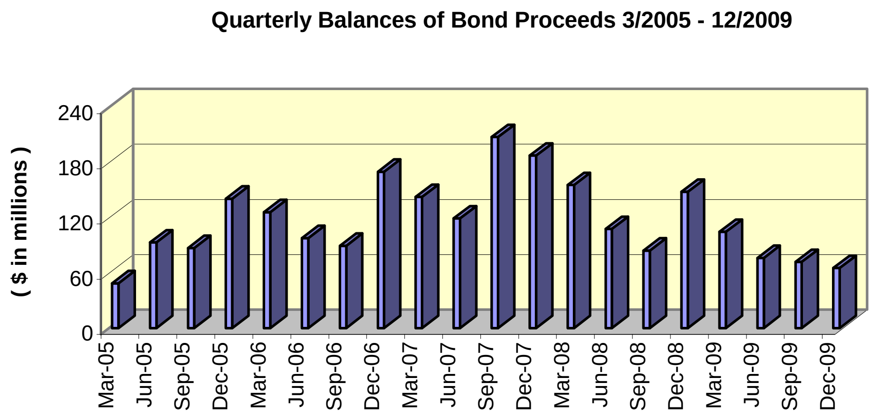
2. **Sinking Fund Commission.** During the 1998 legislative session, the Sinking Fund Commission was reconstituted and given the responsibility of overseeing a program of debt reduction that would be the result of the increased allocation of current revenues to defease or prepay debt. The goal of the Sinking Fund Commission is to reduce debt levels with an increasing appropriation of savings and other revenues to prepay additional debt. The Commission is currently inactive however, the enhanced use of the Rhode Island Capital Fund for Pay As You Go capital financing has reduced issuance of debt for certain new projects in furtherance of the State's goad to moderate its debt burden.

3. **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 $65.4 million in 26 accounts as of December 31, 2009 down from $148.3 million in 30 accounts as of December 31, 2008.

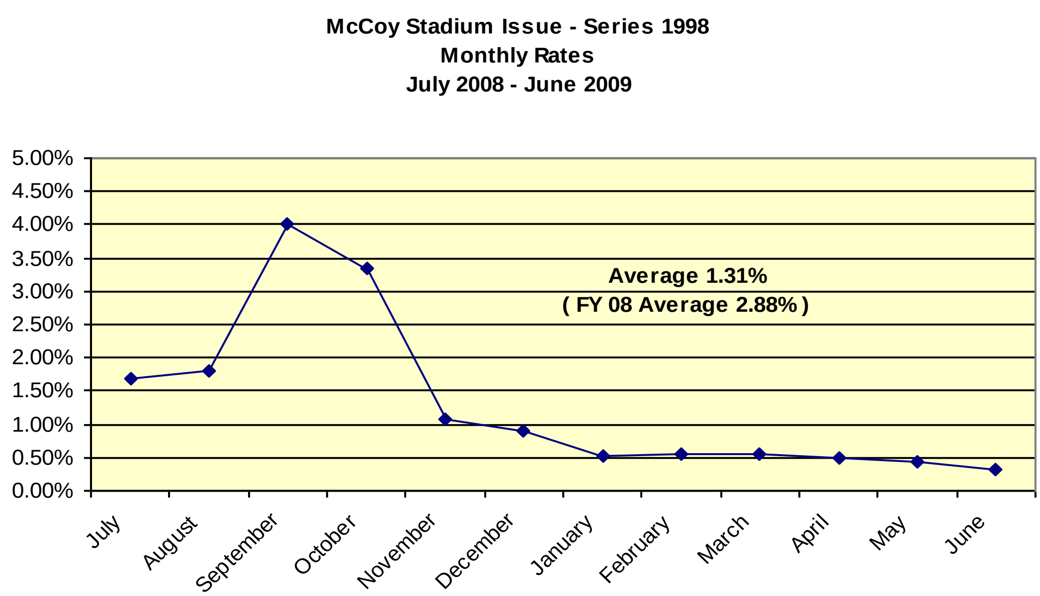
Invested Bond Proceeds By Fund
December 31, 2009

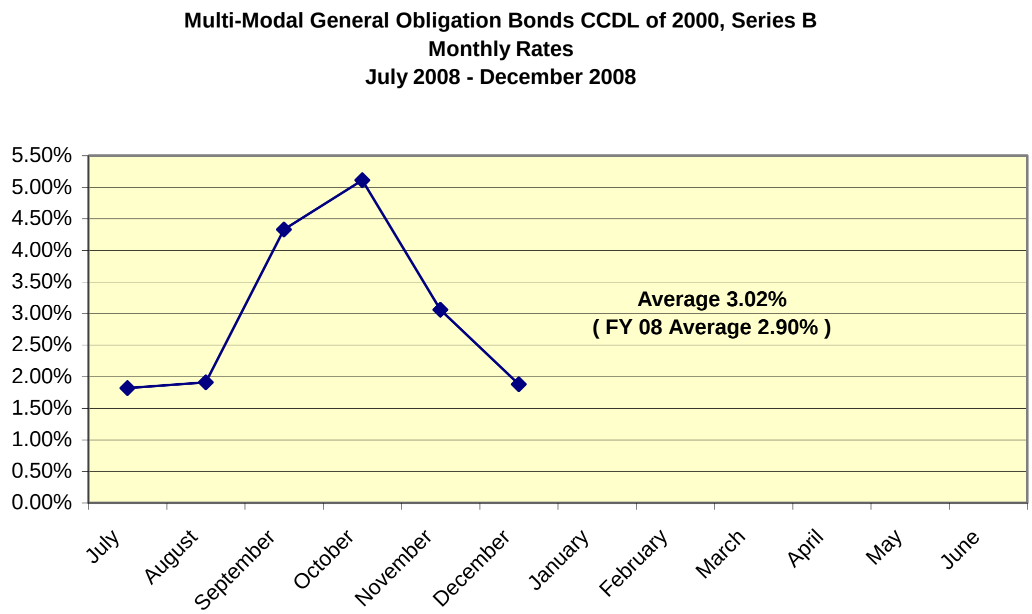
Fund	Amount
Bond Capital Fund	1,109,799.31
G.O. Note 1991 Series B	3,791.71
Bond CCDL 1994 Series A	174,178.93
Bond CCDL 1996 Series A	257,760.13
Capital Development Loan 1997 Series A	345.09
CCDL 1998 Series B	1,749,682.67
Multi-Modal 1999 Series B	2,846.04
Bond Capital CCDL 2000 Series A	951,314.69
Multi-Modal 2000 Series B	2,817.73
CCDL 2004 Series A	7,088,894.86
CCDL 2005 Series C	16,041,608.81
CCDL 2005 Series E	2,425,653.54
CCDL 2006 Series B	22,645.93
CCDL 2006 Series C	6,404,943.63
Non-Taxable G.O. Bond 2007 Series A	704,979.70
Taxable G.O. Bond 2007 Series B	4,005,882.62
Non-Taxable G.O. Bond 2008 Series B	13,548,327.01
Taxable G.O. Bond 2008 Series C	8,498,300.63
Clean Water CCDL 1994 Series A	6,047.31
Capital Development Loan 1997 Series A	11,166.43
Clean Water CCDL 2004 Series A	647,518.83
Clean Water CCDL 2005 Series E	51,692.81
CCDL 1999 Series A	278,095.07
Pollution Control CCDL 2006 Series C	232,530.24
Clean Water 2007 Series A	499,373.25
Pollution Control 2008 Series B	699,221.12
	$ 65,419,418.09

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.



4. Variable Rate Debt Obligations Issued. The State has issued a total of $100.3 million of multi-modal variable rate general obligations bonds: $36.5 million in July 1998, $32.4 million in September 1999 and $31.4 million in July 2000. In addition, the State was also involved in a variable rate financing for McCoy Stadium that was issued by the Economic Development Corporation in July 1998. These floating rate structures 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. 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 for the State. The 1998 and 1999 variable rate bonds were refunded with fixed rate bonds in February 2001 as part of a $118.9 million refunding. The remaining general obligation variable rate bonds were refinanced with fixed rate bonds in December 2008.





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 will be made on December 15, 2010, eliminating any State exposure to variable rate debt.

5. **Municipal Debt Report.** The PFMB published its initial Local Debt Study for cities and towns in 1998. This report demonstrated that the State's debt load can, in part, be attributed to governmental functions assumed at the state level that in other states are assumed at the local or county level. Examples of this include the State's convention center and correctional facilities. This argument implies that Rhode Island's local governments are relieved of a relatively heavy debt burden. Based on the municipal debt report, this is true for the majority of Rhode Island cities and towns. The report showed that, on average, Rhode Island's city and town debt ratios were approximately half of the Standard and Poor's "moderate" benchmark of cities and towns of comparable size in other states, which partially explains the State's high debt ratios. The PFMB publishes the Municipal Debt Report biannually and is expected to publish the next local debt study in December 2011.

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, 2009, dollars in millions, principal amount)

	6/30/2007	6/30/2008	6/30/2009
Tax Supported Debt			
General Obligation Bonds	$ 913.5	$ 997.1	$ 1,036.2
Capital Leases	252.6	226.0	267.1
Convention Center Authority	280.0	271.0	263.8
Economic Development Corporation	147.0	142.6	286.5
R.I.H.M.F.C. Neighborhood Opportunities Housing Program	15.5	18.2	13.2
Refunding Bond Authority	42.7	24.2	6.0
Gross Tax Supported Debt	$ 1,651.3	$ 1,679.1	$ 1,872.8
Agency Payments	(28.9)	(27.8)	(26.6)
Net Tax Supported Debt	**$ 1,622.4**	**$ 1,651.3**	**$ 1,846.2**
State Supported Revenue Debt			
EDC - Providence Place Mall	33.7	32.1	30.4
R.I. Housing	292.5	321.8	285.3
Industrial Recreational Building Authority - Insured Industrial Facilities Corporation	13.2	10.9	14.1
State Supported Revenue Debt	**$ 339.4**	**$ 364.8**	**$ 329.8**
Agency Revenue Debt			
Airport Corporation	$ 308.0	$ 334.8	$ 327.7
Economic Development Corporation	67.8	77.2	94.4
EDC - GARVEE Bonds, Federally Funded	207.8	285.5	427.4
R.I. Housing	5.0	5.0	5.0
Narragansett Bay Commission	444.7	463.2	444.0
Resource Recovery Corporation	16.2	14.5	14.8
State University and Colleges	199.3	195.1	222.6
Turnpike and Bridge Authority	27.8	25.7	23.6
Water Resources Board	8.3	7.5	5.8
Agency Revenue Debt	**$ 1,284.9**	**$ 1,408.5**	**$ 1,565.3**
Conduit Debt			
Clean Water Finance Agency	$ 576.9	$ 631.3	$ 602.6
Health and Educational Building Corporation	1,908.0	2,225.4	2,377.6
R.I. Housing	1,234.5	1,289.6	1,293.7
Industrial Facilities Corporation	105.2	86.1	89.3
Student Loan Authority	889.6	946.8	1,046.3
Water Resources Board	3.0	2.0	1.0
Conduit Debt	**$ 4,717.2**	**$ 5,181.2**	**$ 5,410.5**

Sources: FY 11 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 and Analysis 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 16 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

Issuer	Tax Supported Debt	Revenue Debt (State Credit Support)	Agency Revenue Debt	Conduit Debt
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	
Refunding Bond Authority	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.

How the Debt Issuers Are Related and Evaluated

All debt issued by the State and its agencies is analyzed for institutional investors, individual investors, and providers of credit guarantees including insurance companies and commercial banks. Credit analysts include the major credit rating services (Moody's Investors Service, Standard & Poor's, and Fitch Ratings); broker-dealers and dealer banks which underwrite State bonds; and institutional investors which purchase State bonds (mutual funds, casualty insurance companies, and investment advisors). In the past, such analysis has also been performed by municipal bond insurance companies which had guaranteed many bonds issued by the State (AMBAC, FSA, MBIA, FGIC, and others). Historically, bond insurers provided insurance guarantees for issuers of relatively risk-free municipal debt ("monoline" insurers). However, during the past few years these monoline insurers began guaranteeing securities backed by sub-prime mortgages. These investments have suffered significant losses, reducing the bond insurers' capital and adversely impacting their coveted AAA credit ratings. As of July, 2010, none of the municipal bond insurers was rated AAA by each agency with rates it and only three insurance companies had ratings in the AA category, only one of which is selectively involved in municipal issues. Therefore, underlying credit characteristics and underlying ratings are critical to market access.

One of the factors these analysts use to evaluate debt issued by state agencies is the degree to which the State's general taxes and revenues may be called upon to pay or support the payment of these debts. Tax Supported Debt, for example, is paid directly by State collected taxes and revenues, while Conduit Debt is solely an obligation of a borrower that is not a State agency. Investors do not expect the State to be directly or indirectly responsible for payment of debt service for Conduit Debt.

Each class of debt is defined in Section 2 on page 9. The following discussion presents historical information about the level of such debt.

Tax Supported Debt: FY05 to FY09

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, 2009 with resulting debt ratios. For FY09, the State's Debt to Personal Income ratio of 4.3% and Debt Service to Revenue ratio of 6.0% 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, 2009 is presented in Appendix A.

Table 3-2
Tax Supported Debt: Fiscal Years 2005 - 2009
(dollars in millions, principal amount)

Fiscal Years	2005	2006	2007	2008	2009	CAGR FY 05 - 09
General Obligation Bonds	$ 800.9	$ 842.6	$ 913.5	$ 997.1	$ 1,036.2	6.7%
Capital Leases	224.6	221.5	252.6	226.0	267.1	4.4%
Convention Center Authority	202.9	287.2	280.0	271.0	263.8	6.8%
Economic Development Corp.	128.3	139.0	147.0	142.6	286.5	22.2%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	13.1	18.8	15.5	18.2	13.2	0.2%
Refunding Bond Authority (1)	74.6	60.3	42.7	24.2	6.0	-46.7%
Gross Tax Supported Debt	$ 1,444.4	$ 1,569.4	$ 1,651.3	$ 1,679.1	$ 1,872.8	6.7%
Agency Payments	(55.0)	(29.7)	(28.9)	(27.8)	(26.6)	-16.6%
Net Tax Supported Debt	**$ 1,389.4**	**$ 1,539.7**	**$ 1,622.4**	**$ 1,651.3**	**$ 1,846.2**	**7.4%**
Annual Net Tax Supported Debt Service (2)	$ 147.1	$ 160.4	$ 174.8	$ 185.8	$ 196.7	7.5%
Debt Ratios: (3)						
Annual Debt Service / Revenues (7.5%)	4.7%	4.8%	5.2%	5.2%	6.0%	6.2%
Net Debt / Personal Income (5% - 6%)	3.7%	4.0%	3.9%	3.9%	4.3%	3.8%
Net Debt / Capita	$ 1,305.3	$ 1,453.9	$ 1,540.5	$ 1,571.5	$ 1,757.0	7.7%
Assumptions:						
Revenues (2), (4)	$ 3,111.4	$ 3,308.3	$ 3,361.0	$ 3,580.9	$ 3,270.8	1.3%
Personal Income	$ 37,627.3	$ 38,816.0	$ 41,113.1	$ 42,618.1	$ 42,988.3	3.4%
Population (5)	1,064,439	1,058,991	1,053,136	1,050,788	1,050,788	-0.3%

CAGR = Compound Annual Growth Rate
Source: FY 11 Capital Budget

(1) The Public Building Authority was merged into the Refunding Bond Authority on 7/21/97. Balances and CAGR are for merged entity FY 05 - FY 09.
(2) FY 09 - FY 11 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 are from the U.S. Census Bureau, April 2009.

As the result of an increase in General Obligation debt, Capital Leases, Economic Development Corporation debt and Rhode Island Housing's Neighborhood Opportunities Housing Program debt, total Net Tax Supported Debt increased by a CAGR of 7.4% from FY05 to FY09. These increases were partially offset by a 46.7% CAGR decrease in Refunding Bond Authority debt. State personal income and revenues grew at an annual compound rate of 3.4% and 1.3%, respectively 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 issues debt that will be paid from State taxes and revenues which represents 15.5% of 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: FY10 to FY14

Using figures provided by the State Budget Office, an estimate of the Tax Supported Debt for the FY10 – FY14 period has been developed along with a forecast of certain debt ratios.

Table 3-3
Tax Supported Debt: Fiscal Years 2010 - 2014
(dollars in millions, principal amount)

Fiscal Years	2010	2011	2012	2013	2014	CAGR FY 10 - 14
General Obligation Bonds	$ 1,063.2	$ 1,100.5	$ 1,116.9	$ 1,121.8	$ 1,129.5	1.5%
Capital Leases	273.7	426.4	522.5	478.8	429.7	11.9%
Convention Center Authority	286.0	277.4	267.5	257.2	246.2	-3.7%
Economic Development Corp.	259.9	238.4	217.3	195.3	172.2	-9.8%
R.I.H.M.F.C. Neighborhood Opp. Hsing Prog.	8.4	3.4	-	-		-
Gross Tax Supported Debt	$ 1,891.2	$ 2,046.1	$ 2,124.2	$ 2,053.1	$ 1,977.6	1.1%
Agency Payments	(25.4)	(24.1)	(22.8)	(21.4)	(19.9)	-6.0%
Net Tax Supported Debt	**$ 1,865.8**	**$ 2,022.0**	**$ 2,101.4**	**$ 2,031.7**	**$ 1,957.8**	**1.2%**
Annual Net Tax Supported Debt Service (1)	$ 218.2	$ 219.1	$ 254.3	$ 274.5	$ 277.9	6.2%
Debt Ratios: (2)						
Annual Debt Service / Revenues (7.5%)	7.0%	7.3%	7.5%	7.8%	7.7%	2.2%
Net Debt / Personal Income (5% - 6%)	4.3%	4.6%	4.6%	4.3%	3.9%	-2.2%
Net Debt / Capita	$ 1,775.6	$ 1,924.3	$ 1,999.8	$ 1,933.5	$ 1,863.1	1.2%
Assumptions:						
Revenues	$ 3,112.4	$ 2,985.9	$ 3,391.1	$ 3,515.0	$ 3,629.5	3.9%
Personal Income	$ 43,310.5	$ 43,909.3	$ 45,276.2	$ 47,392.1	$ 49,587.6	3.4%
Population (3)	1,050,788	1,050,788	1,050,788	1,050,788	1,050,788	0.0%

CAGR = Compound Annual Growth Rate
Source: FY 11 Capital Budget

(1) Projected Net Tax Supported Debt Service. FY 11 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, April 2009.

Gross Tax Supported Debt (excludes adjustments for agency payments) is projected to increase from $1,891.2 million in FY10 to $1,977.6 million in FY14.

Table 3-4 shows additional proposed increases in Debt Service Payments for Tax Supported Debt from FY10 to FY14. Historic Structures Tax Credit Fund accounts for the majority of the increase in Total Capital Leases.

Table 3-4
Projected Increase in Debt Service for Tax Supported Debt: Fiscal Years 2010 - 2014
General Obligation Bonds and Capital Leases
(dollars in millions, principal amount)

Fiscal Years	**2010**	**2011**	**2012**	**2013**	**2014**
General Obligation Bonds	$ -	$ 3.0	$ 6.3	$ 9.6	$ 13.1
D.M.V. Technology - C.O.P.'s	1.4	1.5	1.6	1.6	1.7
C.C.A. - Veterans Memorial Auditorium	-	-	0.7	0.8	0.8
Energy Conservation Equipment Leases - P & Z	-	0.6	1.7	1.8	1.9
State Hospital Building Consolidation at Pastore	-	-	0.9	1.0	1.0
Historic Structures Tax Credit Fund	-	-	8.9	17.4	23.3
Energy Conservation Equip. Leases - URI & CCRI	-	1.7	1.8	1.9	2.0
Total Capital Leases	$ 1.4	$ 3.8	$ 15.6	$ 24.5	$ 30.7
Total	**$ 1.4**	**$ 6.8**	**$ 21.9**	**$ 34.1**	**$ 43.8**

Sources: FY 11 Capital Budget.

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 $329.8 million at June 30, 2009, down from $364.8 million at June 30, 2008. 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 3-5 presents the amounts and types of State Supported Revenue Debt for the five years ending June 30, 2009.

Table 3-5
State Supported Revenue Debt: Fiscal Years 2005 - 2009
(dollars in millions, principal amount)

Fiscal Years	2005	2006	2007	2008	2009	CAGR FY 05 - 09
EDC - Collaborative	24.5	-	-	-	-	-
EDC - Providence Place Mall	36.7	35.2	33.7	32.1	30.4	-4.6%
R.I. Housing	273.0	246.1	292.5	321.8	285.3	1.1%
Industrial Recreational Building Authority - Insured Industrial Facilities Corporation	26.0	21.9	13.2	10.9	14.1	-14.2%
Total	**$ 360.2**	**$ 303.2**	**$ 339.4**	**$ 364.8**	**$ 329.8**	**-2.2%**

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 increased by 12.3 million (CAGR of 1.1%) since 2005. When combined with the defeasance of the Blackstone Valley Commission and Narragansett Bay Commission debt, State Supported Revenue Debt decreased by an annual compound rate of 2.2% for the period from FY05 to FY09.

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 Economic Development Corporation is authorized to secure 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.

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 3-6. Only the Revenue Debt of these agencies is presented in Table 3-6, and any other debt is presented in the sections relating to Tax Supported Debt. Table 3-6 presents the amounts and types of Agency Revenue Debt for five fiscal years ending June 30, 2009.

Table 3-6
Agency Revenue Debt: Fiscal Years 2005 - 2009
(dollars in millions, principal amount)

Fiscal Years	2005	2006	2007	2008	2009	CAGR FY 05 - 09
Airport Corporation	$ 269.5	$ 314.1	$ 308.0	$ 334.8	$ 327.7	5.0%
Economic Development Corporation	46.6	65.5	67.8	77.2	94.4	19.3%
EDC - GARVEE Bonds, Federally Funded	186.0	338.4	207.8	285.5	427.4	23.1%
R.I. Housing	5.0	5.0	5.0	5.0	5.0	0.0%
Narragansett Bay Commission	292.7	363.8	444.7	463.2	444.0	11.0%
Resource Recovery Corporation	19.6	20.4	16.2	14.5	14.8	-6.8%
State University and Colleges	183.7	201.7	199.3	195.1	222.6	4.9%
Turnpike and Bridge Authority	31.7	29.8	27.8	25.7	23.6	-7.1%
Water Resources Board	9.8	9.1	8.3	7.5	5.8	-12.3%
Total	**$ 1,044.6**	**$ 1,347.8**	**$ 1,284.9**	**$ 1,408.5**	**$ 1,565.3**	**10.6%**

CAGR = Compound Annual Growth Rate
Source: Treasury Survey of R.I. Quasi-Public Corporations.

The Economic Development Corporation – GARVEE Bonds experienced the largest increase of 23.1%, which maxed out the remaining legislative authorization for the GARVEE Bonds. The second largest increase of 19.3% was from other bonds of the Economic Development Corporation. Next was the Narragansett Bay Commission at 11.0% due to the combined sewer overflow project. The State University and Colleges also increased by 4.9% because of various construction and improvement projects. Overall, Agency Revenue debt grew at a compound annual rate of 10.6% from FY05 - FY09. 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 3-7 is secured by any form of State Credit Support.

Table 3-7
Conduit Debt: Fiscal Years 2005 - 2009
(dollars in millions, principal amount)

Fiscal Years	2005	2006	2007	2008	2009	CAGR FY 05 - 09
Clean Water Finance Agency	$ 504.6	$ 535.8	$ 576.9	$ 631.3	$ 602.6	4.5%
Health and Educational Building Authority	1,519.3	1,659.5	1,908.0	2,225.4	2,377.6	11.8%
R.I. Housing	1,083.2	1,041.9	1,234.5	1,289.6	1,293.7	4.5%
Industrial Facilities Corporation	84.7	98.6	105.2	86.1	89.3	1.3%
Student Loan Authority	803.4	793.9	889.6	946.8	1,046.3	6.8%
Water Resources Board	4.7	3.9	3.0	2.0	1.0	-32.1%
Total	**$ 3,999.9**	**$ 4,133.6**	**$ 4,717.2**	**$ 5,181.2**	**$ 5,410.5**	**7.8%**

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 7.8% from FY05 - FY09. The agencies which experienced the most significant growth in debt were the Health and Educational Building Corporation and the Student Loan Authority with compound annual growth rates of 11.8% and 6.8% respectively. R.I. Housing and the Clean Water Finance Agency debt levels have also been on the rise, each at the slower rate of 4.5%.

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 3-8 presents the amounts of Local Government Debt for the five years ending June 30, 2009. This table does not include the debt of certain regional and municipal authorities including the Bristol County Water Authority, the Foster Glocester Regional School District, Kent County Water Authority, and the Providence Public Building Authority.

Table 3-8
Local Government Debt: Fiscal Years 2005 - 2009
(in millions)

Fiscal Years	**2005**	**2006**	**2007**	**2008**	**2009**	**CAGR FY 05 - 09**
Local Government Debt	$ 1,380.3	$ 1,433.9	$ 1,498.5	$ 1,713.7	$ 1,692.0	**5.2%**

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 the general obligation bonds, revenue bonds, and capital leases of Rhode Island's 39 local governments. During the five years shown in Table 3-8 this debt grew at an average annual rate of 5.2%. Local Debt Studies, issued biennially in 2001, 2003, 2005, 2007 and 2009, indicated that debt levels for Rhode Island cities and towns were relatively low when compared to national indices. Given the inconsistencies among state and local revenue structures, overlapping debt and unavailability of timely data, this report does not draw a comparison of Rhode Island's combined State and local debt with that of other States. The Local Debt Study will be updated in the fourth quarter of calendar year 2011. In light of the availability of published information on cities and towns, the Local Debt Study will continue to be produced on a biennial basis.

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 2009 and 2010. 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 FY10 through FY14, as presented in Table 3-3, indicate that Debt to Personal Income will decrease from 4.3% to 3.9% during this period. These projections also show Debt Per Capita increasing by only 1.2% from $1,775.6 to $1,863.1 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 4.3% in FY09 compares favorably to Moody's 2009 peer group (see Tax Supported Debt herein) average of 4.6%, this ratio is high relative to Moody's 2009 median (includes all states) of 2.5%. Likewise, the State's FY09 Debt per Capita of $1,757.0 compares unfavorably to the current Moody's median at $936, but favorably to the 2009 Peer Group Average of $2,348. 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

	Moody's	S & P	Fitch
Alabama	Aa1	AA	AA+
Alaska	Aa1	AA+	AA+
Arizona	Aa2	AA-	NR
Arkansas	Aa1	AA	NR
California	A1	A-	A-
Colorado	Aa1	AA	NR
Connecticut	Aa2	AA	AA+
Delaware	Aaa	AAA	AAA
Florida	Aa1	AAA	AAA
Georgia	Aaa	AAA	AAA
Hawaii	Aa1	AA	AA+
Idaho	Aa1	AA	NR
Illinois	Aa3	A+	A+
Indiana	Aaa	AAA	NR
Iowa	Aaa	AAA	NR
Kansas	Aa1	AA+	NR
Kentucky	Aa1	AA-	NR
Louisiana	Aa2	AA-	AA
Maine	Aa2	AA	AA+
Maryland	Aaa	AAA	AAA
Massachusetts	Aa1	AA	AA+
Michigan	Aa2	AA-	AA-
Minnesota	Aa1	AAA	AAA
Mississippi	Aa2	AA	AA+
Missouri	Aaa	AAA	AAA
Montana	Aa1	AA	AA+
Nebraska	Aa2	AA+	NR
Nevada	Aa1	AA+	AA+
New Hampshire	Aa1	AA	AA+
New Jersey	Aa2	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	Aa3	AA	NR
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	Aa2	AA	AA
Wisconsin	Aa2	AA	AA
Wyoming	NR	AA+	NR

Rhode Island rating compared to other states:

	Moody's	S & P	Fitch
Above Rhode Island	33	25	28
Same as Rhode Island	12	18	5
Below Rhode Island	3	6	3
NR	1	0	13

Source: First Southwest Company - State Ratings as of 5/11/10.

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).

Table 4-2
Comparison to Peer States
Net Tax Supported Debt to Personal Income

Year	RI	RI National Rank	Moody's Median	Peer State Ave	DE	CT	MA	ME	NH	VT
1999	6.5%	5th	2.0%	5.1%	5.7%	8.7%	7.8%	1.9%	2.3%	4.2%
2000	6.2%	5th	2.2%	4.9%	5.2%	8.1%	8.0%	2.1%	2.0%	3.8%
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%

Source: Moody's Investors Service
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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 1999 - 2006 and its ranking dropped from the 5th 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 2009 the ratio increased to 4.5% giving Rhode Island a ranking of 11th 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

Year	RI	RI National Rank	Moody's Median	Peer State Ave	DE	CT	MA	ME	NH	VT
1999	$ 1,670	5th	$ 505	$ 1,523	$ 1,581	$ 3,131	$ 2,436	$ 418	$ 620	$ 953
2000	$ 1,661	6th	$ 540	$ 1,531	$ 1,544	$ 3,052	$ 2,612	$ 488	$ 567	$ 925
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

Source: Moody's Investors Service
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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
Net Tax Supported Debt Service as a Percent of General Revenues

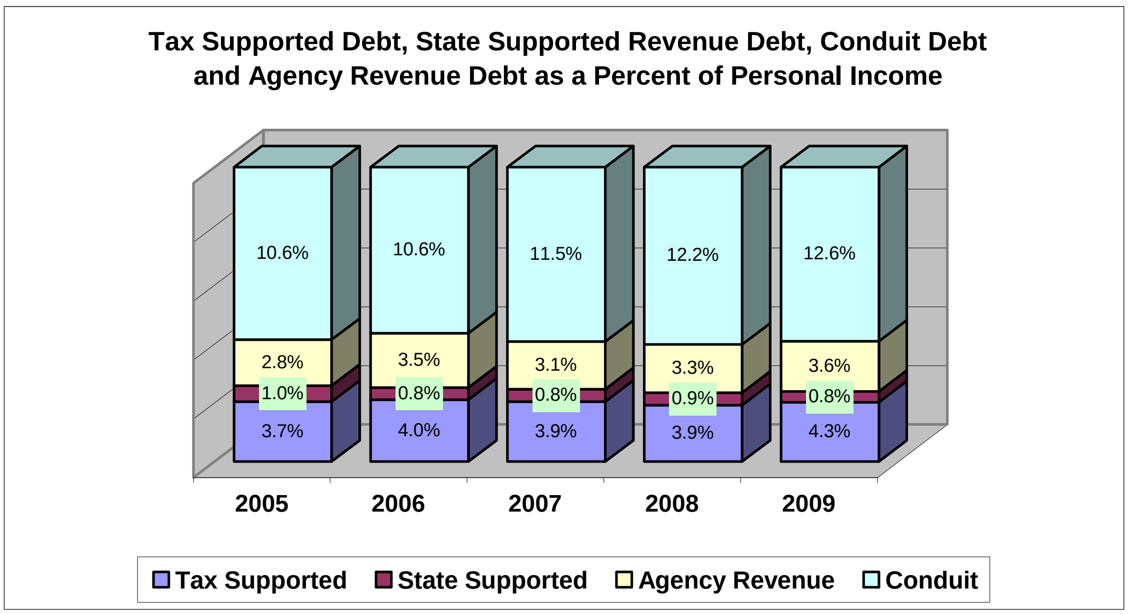
Year	RI
2005	4.7%
2006	4.9%
2007	5.2%
2008	5.2%
2009	6.0%

Source: FY 06 - FY 10 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. 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 18.1% of Personal Income in FY05 to 21.3% in FY09. This increase came as Personal Income grew at the compound annual growth rate of 3.4%.



Section 5

Recommended Priorities and Issues for 2010 and 2011

Based on the findings of this and the preceding Debt Management Reports, the following debt management priorities are recommended for 2010 and 2011.

1. Continued Emphasis on Rating Agency Communication and Debt Management

Rhode Island's improved debt position is the product of stringent policies and fiscal discipline adopted after the State's debt burden peaked in the early '90s. The 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. Continued vigilance is required. Rhode Island's current debt ratings are based on the expectation that the State will continue this debt management course.

The credit guidelines and more conservative debt ratio targets approved by the PFMB in June 2000 provide the structure necessary to achieve further debt reduction while not overly constricting state debt. It is also appropriate, 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.

Municipal Market participants are also concerned with Pension Funding levels of States and the impact of the implementation of GASB Statement 45 related to Other Post Employment Benefits (OPEB). Rhode Island's efforts to reform the retiree health care and pension systems are a positive development. However, more progress needs to be made in this area to manage future liabilities.

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 constrained. Currently, two rating agencies, Fitch Ratings (which downgraded the State in 2008) and Standard & Poor's, have a negative outlook on the State's rating. Moody's Investor's Service which recalibrated their municipal ratings in 2010, currently has a stable outlook on the State's rating. Among the reasons given for the changes in the level and outlook of the State's rating include the severity of the economic downturn, rising unemployment, and declining revenues for FY09 and FY10. 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.

2. More Pay-as-You-Go Funding

In November 2006, the voters approved a constitutional amendment which restricts the use of the Rhode Island Capital Plan Fund solely to fund capital projects. Previous language allowed for the fund's resources to be used for debt service. The multi-year plan of dedicating increased resources towards pay-as-you-go capital projects was modified in past fiscal years to address operating budget deficits and resulted in numerous planned capital projects being deferred. Given the magnitude of the FY 2007 and FY 2008 deficits, the Governor recommended that some of these projects be deferred and/or funded from resources to be made available from the proceeds of the Securitization of Tobacco Master Settlement revenues.

The Governor's proposed Capital Improvement Plan for FY 2011 – FY 2015 reflects the thirteenth year in a comprehensive, yet affordable, asset protection program that will result in the dedication of over $334.4 million of current revenues towards preserving Rhode Island's buildings, roads, bridges, and other assets over the next five years.

3. Continued Diligence in Reporting

The PFMB's reporting responsibilities also should continue to include the review of local government debt every two years based on the expected timing of available information. The PFMB should also report on special projects as warranted. One such project that has been implemented is an integrated debt management system.

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. Most recently, in February 2010, 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 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. RIPEC's Municipal Fiscal Healthcheck was published in April, 2003. 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.

5. Explore Alternative Funding Mechanisms for Major Infrastructure Projects

The State's Capital Budget and Transportation Improvement Plan ("TIP") projects 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. Dedication of additional portions of the gasoline tax to Transportation – when resources permit more of that revenue source to be redirected from the General Fund – will 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. Treasury staff did review the Garvee and Motor Fuel Tax bond issue structures as part of the November 2003, March 2006 and April 2009 issues.

Several states are exploring 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 have also 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. Disclosure Practices and Investor Relations

The Municipal Markets place increasing importance on Issuer Disclosure Information, not only when bonds are issued, but on a continuing basis. It is recommended that the State continue the Investor Relations program initiated by the Treasurer to enhance the participation of Rhode Island "retail" investors in the purchase of State issued debt. 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 and Financial Advisor. Recent developments in the monoline insurance industry 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. A training program for staff in Treasury and Administration is recommended to institutionalize the practices which have been developed in recent years. This is especially relevant in light of the emergence of crossover taxable buyers in the municipal market as well as issuer oversight of the Securities and Exchange Commission such as with the State of New Jersey pension disclosure issues.

7. Responding to the Rapidly Changing Municipal Bond Market

The global credit crisis of 2008 has 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.

8. American Recovery and Reinvestment Act of 2009

The American Recovery and Reinvestment Act (ARRA) of 2009 included many municipal bond provisions that can benefit the State and its agencies and municipalities. The Office of the General Treasurer has been involved in evaluating the applicability of Build America Bonds, Recovery Zone Bonds and Qualified School Construction Bonds. The Build America Bonds in particular have had a profound impact on the municipal market, affording tax exempt issuers access to a new universe of investors in taxable debt. 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.

9. Monitor changes in the Municipal Market resulting from passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

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.

EXHIBIT A

Schedule of Tax Supported Debt

EXHIBIT B

Recent Credit Rating Reports

EXHIBIT C

Schedule of Debt Issuances