ABOUT BONDS

In light of the bond on the ballot in this election, we are providing background information regarding the state's current bond debt, as well as the impact that approval of Proposition 41 could have within the framework of these state obligations and the costs of paying them off over time.

What are Bonds? Bonds are a form of long-term borrowing that the state uses to raise money for infrastructure projects. The state sells bonds to investors and agrees to repay the investors, with interest, according to a specified schedule.

Why Are Bonds Used? Projects such as roads, educational facilities, prisons, parks, office buildings, and housing for veterans involve large dollar costs, and are used over many years. The use of bonds helps to fund the initial large dollar costs, which would be hard to fund out of day-to-day operating revenues. Also the repayment of these bonds over time means that future taxpayers who benefit from the facilities will help to pay for them.

What Types of Bonds Does the State Sell? General Obligation Bonds are the most significant type of bonds and are largely repaid from the state's unrestricted general tax revenues. These bonds have to be approved by the voters, and their repayment is effectively guaranteed by the state. The bonds proposed in Proposition 41 are general obligation bonds.

There are also ***Revenue Bonds***, repaid from a designated revenue stream—such as bridge tolls*, and* ***Lease-Revenue Bonds***, repaid from lease payments by state agencies using the leased facilities. Neither type requires voter approval, nor is their repayment guaranteed by the state.

What Are the Direct Costs of Bond Financing? The state must repay the principal of the bonds over time to the investors until the bonds are fully paid off, plus annual interest costs. The interest cost of repaying bonds depends primarily on the current interest rate and the time period over which the bonds have to be repaid. It's expected that the bonds proposed by Proposition 41 would be sold over a 30-year period (similar to how homeowners pay off their 30-year home mortgages) at an expected interest rate of 5%.

Amount of General Fund Debt. The state currently has about $85 billion of infrastructure bonds outstanding, almost 90% of which are general obligation bonds. In addition, about $33 billion of infrastructure bonds have been approved by the voters and are expected to be sold in the coming years as additional projects need funding. From now until 2020, the annual bond repayments, both principal and interest, are expected to rise from over $5 billion to over $7 billion.

This Election's Impact on the Debt Servicing. One indicator of the state's debt burden is the portion of the state's annual general revenues that must be set aside for debt-service payments. The current amount of the state's debt is relatively high in proportion to its unrestricted general revenue. Proposition 41 is requesting approval of $600 million of general obligation bonds to fund multifamily housing and services for low-income veterans. This measure, if approved, would increase the amount of the state's debt, and its annual debt-servicing burden, only very minimally.