NEW JERSEY STATE LEGISLATURE
★ *Office of* LEGISLATIVE SERVICES ★

LEGISLATIVE BUDGET
AND FINANCE OFFICE
(609) 847-3105

MEMORANDUM

TO: Tom Neff
Budget Director
Senate Republican Office

FROM: Thomas Koenig
Legislative Budget and Finance Officer

DATE: January 29, 2024

SUBJECT: Debt Reduction Strategies

You have requested a comparison of the State debt service impacts of the $500 million debt defeasance announced by the Department of the Treasury on January 18, 2024 and a counterfactual consisting of the reduction by $500 million of the November 2023 issuance of $1.25 billion in Transportation Trust Fund Authority bonds. I hope you will find the following discussion helpful.

New Jersey Debt Defeasance and Prevention Fund: Since 2021, three laws deposited a combined $9.25 billion into the New Jersey Debt Defeasance and Prevention Fund (P.L.2021, c.125; P.L.2022, c.18; and P.L.2023, c.68). Fund balances are to be used to retire and defease State debt and to fund capital projects on a pay-as-you-go basis rather than through the issuing of additional State debt. The State Treasurer is required to submit to the Joint Budget Oversight Committee a report on any debt defeasance or retirement that was executed using New Jersey Debt Defeasance and Prevention Fund resources.

FY 2024 Debt Defeasance: On January 18, 2024, the State Treasurer submitted the required report on the FY 2024 debt defeasance and retirement to the Joint Budget Oversight Committee. The State Treasurer informed that some $659.6 million in combined principal and interest payments was defeased at a cost of $499.5 million. The report breaks out the debt service savings by fiscal year, which are reproduced in the comparison chart on page 3 of this memorandum.

Netting out principal repayments and interest payments required prior to the bonds' respective call dates yields $160.1 million in net interest savings to the State through FY 2037, according to the State Treasurer. It is this amount to which the net savings of counterfactual alternative uses of $500 million in New Jersey Debt Defeasance and Prevention Fund balances must be compared.

Importantly, the Department of the Treasury specified that it considered for defeasance outstanding debt that was: a) payable from only the State's General Fund or Property Tax Relief Fund; and b) callable at the State's direction. The strategy, therefore, excluded bonds whose debt service is paid from other State funds, such as the Transportation Trust Fund. This limitation is consistent with the laws making deposits into the New Jersey Debt Defeasance and Prevention Fund, which delegate the authority to determine the debt defeasance strategy to the State Treasurer.

Transportation Program Bonds, 2023 Series BB: In November 2023, the Transportation Trust Fund Authority issued $1.25 billion in Transportation Program Bonds, 2023 Series BB to finance transportation capital projects in the State. Debt service payments on the bonds through maturity in FY 2050 will total $2.46 billion, composed of $1.25 billion in principal repayments and $1.21 billion in interest payments.

In addition to the bonds' $1.25 billion par amount, the Transportation Trust Fund received $69.0 million in original issue premium, producing $1.32 billion in fund resources. Of that amount, more than $1.31 billion was deposited into the Transportation Trust Fund for capital projects, while $3.9 million was used for the underwriters' discount and $887,750 for the cost of issuance (bond ratings, printing, legal and trustee funds, etc.).

Comparing FY 2024 Debt Defeasance and Transportation Bond Counterfactual: As noted above, the Treasury stated that using $500 million in New Jersey Debt Defeasance and Prevention Fund deposits in the FY 2024 debt defeasance yielded $160.1 million in net debt service savings.

Below, the Office of Legislative Services estimates the debt service savings that could have been realized if the $500 million had instead been used to reduce the $1.25 billion bond issuance by the Transportation Trust Fund Authority in November 2023.

For purposes of this analysis, the OLS makes a simple assumption: the $500 million (or 40 percent) par amount reduction for the transportation program bonds to $750 million would have lowered debt service payments in each fiscal year proportionately by 40 percent. In actuality, the November 2023 bond issuance consisted of several serial bonds and two term bonds with different maturities. Thus, the Department of the Treasury could have chosen to structure a $750 million debt issuance in many different ways, thereby producing different debt service savings outcomes.

Based on the simplifying assumption, the OLS estimates that nominal net savings to the Transportation Trust Fund from reducing the November 2023 bond issuance by $500 million would have approximated $456.4 million. This contrasts with $160.1 million in net savings from the FY 2024 debt defeasance.

In addition, a smaller bond issuance could have also affected the underwriters' discount and the cost of issuance. At $1.25 billion, the underwriters' discount was $3.9 million and the cost of issuance $887,750. The OLS, however, has no informational basis to estimate the extent to which a decreased issuance amount would have lowered the underwriters' discount and the cost of issuance, and how the savings would have compared to the unknown cost of services the State purchased in implementing the FY 2024 debt defeasance.

As a final observation, because of the funding mechanism for the Transportation Trust Fund, the FY 2024 debt defeasance savings and the hypothetical reduction in Transportation Trust Fund debt service do not return the same budgetary effects, which may have been a factor in the selection of the debt reduction strategy.

Specifically, the FY 2024 debt defeasance reduces the debt service appropriations in annual appropriations acts through FY 2037, freeing up State resources. In contrast, the amount to be raised from taxpayers each year in support of all Transportation Trust Fund expenditures is prescribed by a statutory formula that does not consider debt service obligations. Therefore, any reduction in Transportation Trust Fund debt service has the effect of increasing the amount of dedicated Transportation Trust Fund revenue allocated for pay-as-you-go capital funding. All other factors being equal, no additional State resources would be freed up for other, non-transportation purposes. Nevertheless, lower Transportation Trust Fund debt service improves the financial condition of the Transportation Trust Fund, and thus of the State. As a result, different policy choices regarding the funding of capital projects may become possible in the future.

Comparison of Debt Service Savings:
FY 2024 Debt Defeasance and Counterfactual Transportation Program Bonds Principal Reduction

Fiscal Year	Debt Service Savings: FY 2024 Debt Defeasance	Estimated Debt Service Savings: $500M Principal Reduction, 2023 Transportation Program Bonds
FY 2024	$42,940,000	$13,740,851
FY 2025	$26,988,000	$25,367,725
FY 2026	$72,438,000	$25,367,725
FY 2027	$68,943,000	$25,367,725
FY 2028	$51,477,000	$25,367,725
FY 2029	$22,842,000	$25,367,725
FY 2030	$12,846,000	$25,367,725
FY 2031	$12,846,000	$25,367,725
FY 2032	$12,846,000	$41,721,725
FY 2033	$104,521,000	$41,722,025
FY 2034	$78,368,000	$41,721,461
FY 2035	$78,369,000	$41,721,925
FY 2036	$51,444,000	$41,723,325
FY 2037	$22,781,000	$41,723,325
FY 2038	$0	$41,721,625
FY 2039	$0	$41,721,825
FY 2040	$0	$41,723,225
FY 2041	$0	$41,723,025
FY 2042	$0	$41,722,425
FY 2043	$0	$41,722,425
FY 2044	$0	$41,721,825
FY 2045	$0	$41,723,325
FY 2046	$0	$41,723,325
FY 2047	$0	$41,722,225
FY 2048	$0	$41,721,225
FY 2049	$0	$41,722,565
FY 2050	$0	$41,723,205
Total Debt Service Savings	**$659,649,000**	**$984,040,962**
Less Defeasance Cost or Principal Reduction	$499,545,000	$500,000,000
Total Net Savings	**$160,104,000**	**$484,040,962**
Less Estimated Reduced Original Issue Premium	$0	$27,613,302
Final Total Net Savings	**$160,104,000**	**$456,427,661**