THE COMMONWEALTH OF MASSACHUSETTS

EXECUTIVE OFFICE FOR

ADMINISTRATION AND FINANCE

STATE HOUSE ▪ ROOM 373 BOSTON, MA 02133

Friday, December 6, 2024

1:00 p.m.

A meeting of the Debt Affordability Committee was held on November 22, 2024. In accordance with Section 20 of Chapter 20 of the Acts of 2021, as extended by Chapter 107 of the Acts of 2022, this meeting will be conducted, and open to the public, via Zoom and Teleconference.

Zoom URL: https://us02web.zoom.us/j/83935411857?pwd=o0ViLM1tc6nFZpMbxuM9gNySafQYhm.1

Meeting ID: 839 3541 1857; **Passcode**: 040354

Teleconference line: 1-646-558-8656; **Passcode:** 040354#

Minutes:

The meeting was called to order at 1:03 pm

Board members comprising a quorum:

Kaitlyn Connors, Chair, Executive Office for Administration & Finance
Martin Benison, Appointee of the Treasurer
Pauline Lieu, Office of the Comptroller
Sue Perez, Office of the Treasurer and Receiver-General
Michelle Scott, Massachusetts Department of Transportation
Catherine Walsh, Appointee of the Governor

Others in attendance:

Representative Michael J. Finn, Chair of the House Bonding, Capital Expenditures, and State Assets Committee
Senator Edward J. Kennedy, Chair of Bonding, Capital Expenditures, and State Assets Committee
Peter DeGrandis, Joint Committee on Bonding, Capital Expenditures and State Assets
Aidan Bettencourt, Office of State Representative Michael Finn
Chris Czepiel, Senate Committee on Ways and Means
Josh Tavares, Office of Senator Ryan Fattman
Michael LaFlamme, Office of State Representative Michael Finn
Cory Bannon, Office of the Treasurer and Receiver-General
Daniel Aldridge, Office of the Treasurer and Receiver-General
Christina Marin, Office of the Treasurer and Receiver-General
Timur Kaya Yontar, Executive Office for Administration and Finance

Minutes:

Ms. Connors called the meeting to order and conducted the roll to establish quorum. She then moved to the first item of business which was approval of the minutes from December 4, 2024, committee meeting. Upon a motion made by Ms. Scott and duly seconded by Ms. Walsh, the minutes were approved unanimously.

Ms. Connors then moved on to the next item on the agenda: DAC Modeling Review. She reviewed the upcoming DAC schedule and noted that the next and final meeting was currently scheduled for December 13, 2024.

Ms. Connors then reviewed the topics that would be covered in this meeting, which included a review of updated modeling findings and preliminary recommendation discussions.

Ms. Connors provided an overview of the proposed assumptions used in the modeling that would be presented, starting with revenue growth and then moving on to interest rates, debt structuring (interest only period, level principal vs. level debt), premium and bond issuance timing.

Ms. Connors noted that because premium was being factored into these modeling scenarios, the interest rates were being held at 5% which was the presumed bond coupon based on actual practice. Ms. Connors noted that if interest rates were based on yield – not coupon – the model would overstate the pricing benefit the Commonwealth would be getting. Ms. Perez confirmed this was the case and stated that this prevents “double dipping” of presumed bond pricing benefits.

Ms. Lieu asked a clarifying question about level debt service vs. level principal. Ms. Perez responded by explaining the difference and confirmed that level debt service aligned with current practice. Ms. Perez noted that this approach guards against backloading principal.

Ms. Connors pointed out that the model had been adjusted to align bond issuance timing with typical Commonwealth timing, noting that the last bond issuance associated with spending in any given fiscal year, typically occurs at the beginning of the next fiscal year. Mr. Benison asked a couple of clarifying questions related actual bond issuance timing to which Ms. Perez responded. Ms. Walsh also asked a clarifying question about the impact this adjustment makes. Ms. Perez responded that without this adjustment the model would have overstated the amount of debt that was going to be issued in the first year of the modeling period, noting the adjustment was about right sizing the starting year of the model.

Ms. Connors then reviewed the modeling results of four scenarios that focused on premium. She noted the model provided estimates for the maximum amount of bond cap growth that could be afforded while remaining under the DAC’s affordability targets assuming 11%, 10% , 7.8% and 3.1% bond premium going forward. Annual revenue growth was set at the conservative 3.2% growth rate in all scenarios. Ms. Connors stated that the modeling focused on premium because preliminary modeling suggested the statutory Direct Debt Limit was the constraining factor of this year’s analysis, and the premium assumptions most directly impacted direct debt.

Ms. Connors reviewed charts that graphically depicted the results. In all four scenarios, projected debt service remained well within debt service policy limits. Ms. Connors noted that when she stress-tested the 10% and 7.8% premium scenarios which assumes revenue only grows by 1.6% annually, debt service policy limits are breached in 2047 and 2049, respectively – well outside the ten year time horizon that the Committee focuses on.

The Committee then discussed next steps for finalizing their recommendation. Ms. Scott asked for confirmation about the timing for voting on the recommendation. Ms. Connors confirmed the vote was scheduled for the December 13, 2024 meeting.

Mr. Benison asked a clarifying question about the Committee’s recommendation Ms. Connors responded that the Committee’s recommendation related to the amount of capital spending for the upcoming fiscal year, which is supported with bonds. Ms. Perez confirmed accuracy.

Mr. Benison recommended that the Committee establish a guiding policy or statement about why its focus is largely on the 10-year horizon. He then proposed that the following paragraph be incorporated into the final recommendation letter in some way. He said it was meant as a first draft and that he was open to feedback and edits. He also mentioned that he had separately sent this paragraph just to Ms. Connors ahead of the meeting, being mindful of open meeting laws.

"The committee recommends the maximum amount of general obligation debt the Administration should consider issuing in the subsequent fiscal year. While the committee' s recommendation reflects a recommendation for the subsequent fiscal year in considering that recommendation, the committee models debt service for 30 subsequent years under 3 sets of assumptions, moderate, conservative and stress or very conservative model. While the committee looks at the impact of its recommendation for 30 years, due to the uncertainty of long-term assumptions regarding tax revenues and interest rates in the municipal market the committee's focus is on the next 10 years. The committee's policy is to adopt a recommendation that would lead to debt service not exceeding 7% of the budget and direct debt as defined not exceeding the cap on direct debt over the next 10 years.

Mr. Benison then reiterated that including some guiding principle statement was a way to formally memorialize what the Committee has been discussing.

Ms. Connors agreed that having a statement like this would make sense as a way to illustrate that the Committee is thinking long term about predictable rate of issuance and bond cap growth. While the Committee is only making a recommendation for the upcoming fiscal year, it factors in reasonable assumptions about future need to ensure future flexibility is preserved.

Ms. Perez agreed that all of these concepts should be clearly laid out in the formal recommendation letter. She also recommended that the letter include an explanation of the scenarios that we run to understand the long term implications, and an acknowledgement that the committee re-examines its analysis each year.

Ms. Connors noted that the Committee provides a lot of detail in the accompanying slide deck that goes with the letter, but agrees the key analysis used to inform the decision should be included in the letter as well. She surmised that the letter was probably more read than the deck.

Ms. Perez stated that the main finding is that the direct debt limit is the constraining factor and when we just miss hitting it, we fall well short of the 7% and 8% debt service thresholds.

Ms. Connors outlined the format of last year's recommendation letter and noted the structure used could be adapted to add the additional information discussed today. She noted that she would incorporate Mr. Benison's language into the letter. She also acknowledged that his statement would appear in the minutes for reference.

Mr. Bension asked a clarifying question about the bond issuance timing 80%/20% split. Ms. Perez responded that the model is really just shifting the timing of issuances, which prevents the model from overstating the amount of debt we issue in year 1.

Ms. Perez requested that the definition of "bond cap" be included in the letter.

Ms. Lieu asked how bond refundings come into play. Ms. Connors replied that the model does not assume any refunding occurs as refunding opportunities are hard to predict. Ms. Perez noted that any savings from refundings would be spread over the remaining life of the bonds so the debt service impact in any given year would be relatively small.

Ms. Lieu recommended the committee define terms like special obligation bonds as well.

Ms. Connors asked the Committee for feedback on the bond cap recommendation amount and stated that she was comfortable with both the +$107M (based on 10% premium) and the +$114 M (based on the 11% premium).

Ms. Scott noted that the Committee had discussed a soft two-year recommendation in earlier meetings.

Ms. Connors confirmed that it was something the Committee had discussed and that she was supportive of including a soft recommendation.

Ms. Walsh asked what the advantage of a soft 2-year recommendation would be. Ms. Connors stated that it would better align with the current CIP cycle approach: in even year's there is a full update and in odd years the Administration takes a "light touch" with a goal of limiting changes to technical adjustments.

Mr. Benison noted that Committee modeling assumes that bond cap growth continues at a fixed growth amount in all out years and that it is reasonable to include in the letter that for planning purposes the model assumes some amount of bond cap growth in Year 2 and beyond.

Ms. Perez said that the Committee could state that we have more confidence in the year 2 growth amount, than, for example, the year ten amount.

Ms. Connors said she would work to incorporate the feedback on the "soft" year 2 recommendation into the letter, as well as all other feedback discussed today. She said she would take the lead in drafting the letter and will circulate the draft to the group for feedback. She noted that feedback should be sent just to her.

She asked if the Committee would like to add another meeting to the schedule. The Committee did not feel strongly about it at this point in time. Mr. Benison said he would have difficulty being able to make another meeting. Ms. Connors said she would reach out in a day or so to survey members on whether they felt an additional meeting was warranted. If there was a desire, she would work to schedule an additional meeting.

Ms. Scott moved a motion to adjourn the meeting, which was seconded by Ms. Walsh. The meeting was adjourned at 2:07 pm.