Debt FAQ

Frequently asked questions about Pennsylvania's debt

Q: Why does Pennsylvania borrow money?

Article VIII of the state constitution lays out several purposes for which the commonwealth can directly incur debt:

- To suppress insurrection,
- For disaster relief,
- To manage cash flow during the fiscal year with tax anticipation notes,
- To refund and refinance existing debt,
- For purposes approved by the voters in referenda, and
- For the approved capital budget.

The large majority of the commonwealth's outstanding direct debt is for the **capital budget**, which provides for the construction, rehabilitation, renovation and improvement of buildings and facilities. Because these assets are used over many years, the commonwealth usually issues bonds to spread the costs over the useful life of the asset.

In addition to capital budget debt, the commonwealth has borrowed money for **disaster recovery** for the 1972 and 1996 floods, and **voter authorized debt** supports priorities like water and sewer infrastructure, environmental protection and farmland preservation, and veterans' benefits.

Over the years, policymakers have addressed important state priorities by creating separate authorities or agencies, some of which have the ability to issue debt. These entities, on occasion, have issued debt on behalf of the commonwealth. While this debt does not have the same general obligation pledge of the commonwealth's full faith and credit used for direct debt, the debt service is often paid through specific revenues dedicated by law or through appropriations made each year by the General Assembly. Due to its intrinsic link, the burden of authority debt issued on behalf of and paid for by the commonwealth is also important to consider when thinking about the full scope of Pennsylvania's debt use.

Q: Does Pennsylvania borrow to pay for its budget, like the U.S. government?

Generally, no, but with caveats.

Shifting Costs to Independent Authorities

The Pennsylvania Constitution requires a balanced operating budget and limits the things for which the commonwealth can directly borrow. Combined, these provisions do not allow the commonwealth to balance its budget by direct borrowing. However, the constitutional rules for direct debt do not constrain authorities and other instrumentalities created by the General Assembly in the same way, which leads to an exception to the general rule.

Because authorities are not subject to the same constitutional restrictions, the General Assembly periodically has used authorities' borrowing capacity to solve varying types of budgetary challenges. Some examples include requiring the Pennsylvania Turnpike Commission to contribute resources to fund transportation needs (funded through increased borrowing by the commission), repaying and refinancing a federal unemployment compensation loan incurred over the Great Recession through the Pennsylvania Economic Development Financing Authority, or switching from annual appropriations to borrowing via the Commonwealth Financing Authority for a number of years to reimburse school districts for construction costs.

In the most direct example from the 2017/18 fiscal year, the General Assembly enacted legislation to direct the Commonwealth Financing Authority to borrow $1.5 billion, backed by the tobacco settlement payments and the sales and use tax (and later, the cigarette tax). The bond proceeds were deposited in the General Fund to help resolve a single year's budgetary shortfall.

While legal distinctions exist between a debt of the commonwealth and a debt of an authority, the practical reality is that the General Assembly has engaged in borrowing to balance the budget in increasingly direct ways. Though authority debt was used for many years to shift costs or support specific activities with alternative funding, the 2017/18 tobacco settlement debt provided revenue directly into the General Fund to pay for expenses – a significant departure from past practices.

Cash Flow Borrowing

Aside from these activities, the Pennsylvania constitution allows for temporary borrowing within a fiscal year to manage **cash flow**. Much of the commonwealth's tax revenues are paid in March and April, but expenses are incurred throughout the fiscal year.

If necessary, the commonwealth can borrow through the public bond market to ensure enough cash is on-hand to pay the bills earlier in the year until the major revenue months arrive. This kind of debt, known as tax anticipation notes, must be repaid by the end of the fiscal year and can only be paid from current year revenues.

While tax anticipation notes used to be common, the Treasurer and the Secretary of the Budget migrated to less expensive cash management tools in recent years, such as internal borrowing and lines of credit.

Q: Does Pennsylvania have a debt limit?

Yes, Pennsylvania has a debt limit, but only for certain kinds of debt. Other restrictions come into play on related issues.

Constitutional Debt Limit

The state constitution limits the amount of capital budget debt that can be incurred to 1.75 times the average annual tax revenues for all funds over the previous five fiscal years as certified by the Auditor General during the year. As of the latest certification in August 2021, the debt limit is around $75.3 billion. Pennsylvania's outstanding net capital budget debt of $9.73 billion is only 12.9% of the constitutional limit; however, the budget could not support the debt service requirements of a debt load near the full constitutional limit.

Annual Capital Budget Limits

Along with the constitutional limit on total capital budget debt, the annual capital budget act specifies how much new principal debt can be incurred in that fiscal year for capital projects until the next capital budget is enacted. The 2019/20 capital budget enacted in May 2020 was $1.01 billion.

2019/20 Capital Budget – Enacted May 2020	
Category	**Debt Authorized**
Public Improvement Projects – Buildings and Structures	$550 million
Public Improvement Projects – Furniture and Equipment	$10 million
Transportation Assistance Projects	$175 million
Redevelopment Assistance Projects	$275 million
Flood Control Projects	$0
Total	**$1.010 billion**

The General Assembly did not pass a capital budget in 2020/21, and, at present, has not passed a capital budget for the 2021/22 fiscal year, though the Pennsylvania Constitution requires the General Assembly to adopt a capital budget for the ensuing fiscal year. The commonwealth pays for capital projects on a cash flow basis, so continued delay in passing a capital budget that authorizes debt to be issued could eventually impact the commonwealth's ability to pay bills for work already completed.

Redevelopment Assistance Capital Program Limit

The Redevelopment Assistance Capital Program (RACP) is a program within the capital budget that provides support for the acquisition and construction of regional economic, cultural, civic, recreational and historical improvement projects. RACP debt is subject to a separate statutory limit.

The RACP debt limit constrains the maximum amount of debt that can be outstanding at any time. The relevant law setting forth the limit generally falls within the Capital Facilities Debt Enabling Act, though the General Assembly has moved the limit to other parts of the law. Currently, the limit is contained within Act 25 of 2020, which set the 2019/20 capital budget.

Under Act 25's schedule, the maximum amount of RACP debt that can be outstanding is declining each fiscal year in $50 million increments, down to a final limit of $3.1 billion. For 2021/22, the limit will be $3.15 billion current amount outstanding.

Non-Capital Budget Limits

The constitution does not place any overall limit on long-term debt for the non-capital purposes - insurrection suppression, disaster relief, or voter-approved programs. In these cases, the enabling legislation passed by the General Assembly or the referenda approved by voters sets the maximum amount that can be borrowed.

Q: What is Pennsylvania's bond rating?

The commonwealth received the following ratings for a general obligation bond issuance in the spring of 2021:

Rating Agency	Rating
Fitch	AA-
Moody's	Aa3
S&P	A+

The ratings are the 4^{th}-5^{th} highest in the schema used by the rating agencies for municipal bond debt.

Each of the major ratings agencies downgraded the commonwealth's debt over a number of years following the Great Recession. In their opinion, Pennsylvania's finances will continue to be strained because of slow revenue growth and increasing mandated costs. These pressures limit the ability of the commonwealth to deal with unexpected fiscal issues, which can increase credit risk.

Credit downgrades matter to the extent that it leads investors to require a higher interest rate when the commonwealth issues debt, which would increase the debt service paid each year. Other market factors can have a greater impact in determining the interest rates besides the bond rating, but it's important to note that both short- and long-term budgetary decisions affect the commonwealth's borrowing activities.

Q: How much debt does Pennsylvania have outstanding?

Net outstanding general obligation debt as of June 30, 2020 was approximately $10.75 billion.

According to the latest official statement prepared for the most recent bond issuance, there are $5.89 billion in other obligations (primarily lease or authority debt) that is secured in whole or part by annual appropriations in the budget in addition to the commonwealth's general obligation debt.

Q: How much does Pennsylvania spend on debt service?

For 2019/20, debt service for general obligation debt totaled $1.331 billion.

The General Fund pays for the large majority of debt service costs for general obligation debt through an annual appropriation to the Treasury Department. The Motor License Fund supports debt service for highway and bridge debt and a handful of special funds also help pay for debt costs associated with specific items.

Debt service, leases and other payments for obligations that are secured by appropriations were an estimated $424 million.

For authority debt issued on behalf of the commonwealth, transfers from sales and cigarette taxes have become a primary source of revenue for debt service payments, with the required amounts being regularly transferred to restricted accounts. In addition, the Motor License Fund and the Pennsylvania Gaming Economic Development and Tourism Fund contribute toward paying components of these obligations.

Q: For how long does Pennsylvania typically borrow?

Generally speaking, the commonwealth issues 20-year bonds. For capital projects, the state constitution requires the debt to be paid back within the useful life of the asset and the debt must also begin to be paid off within one-tenth of the term of the debt. This means that some projects with a shorter lifespan will be amortized within a shorter time frame.

Q: How does Pennsylvania's debt level compare with other states?

A meaningful comparison of relative debt loads requires adjustment for the different wealth and population levels across the country. The annual State Debt Medians report prepared by Moody's Investors Service makes these adjustments to provide apples-to-apples comparisons amongst states.

The following table summarizes Pennsylvania's position relative to other states, according to the 2021 Moody's report, which analyzed 2020 data.

Metric	Pennsylvania	National Median	National Average	Pennsylvania Rank
Net tax-supported debt per capita	$1,448	$1,039	$1,535	19th
Net tax supported debt as a % of 2020 personal income	2.3%	1.9%	2.5%	20th
Net tax supported debt as a % of 2020 state GDP	2.37%	2.04%	2.43%	20th