

P U B L I C H E A R I N G
before
SENATE REVENUE, FINANCE AND APPROPRIATIONS COMMITTEE
on
SENATE CONCURRENT RESOLUTION NO. 3027

(A Concurrent Resolution proposing to amend Article VIII,
Section II, paragraph 3 of the Constitution of the State of New Jersey)

Held:
July 7, 1983
Room 114, State House Annex
Trenton, New Jersey

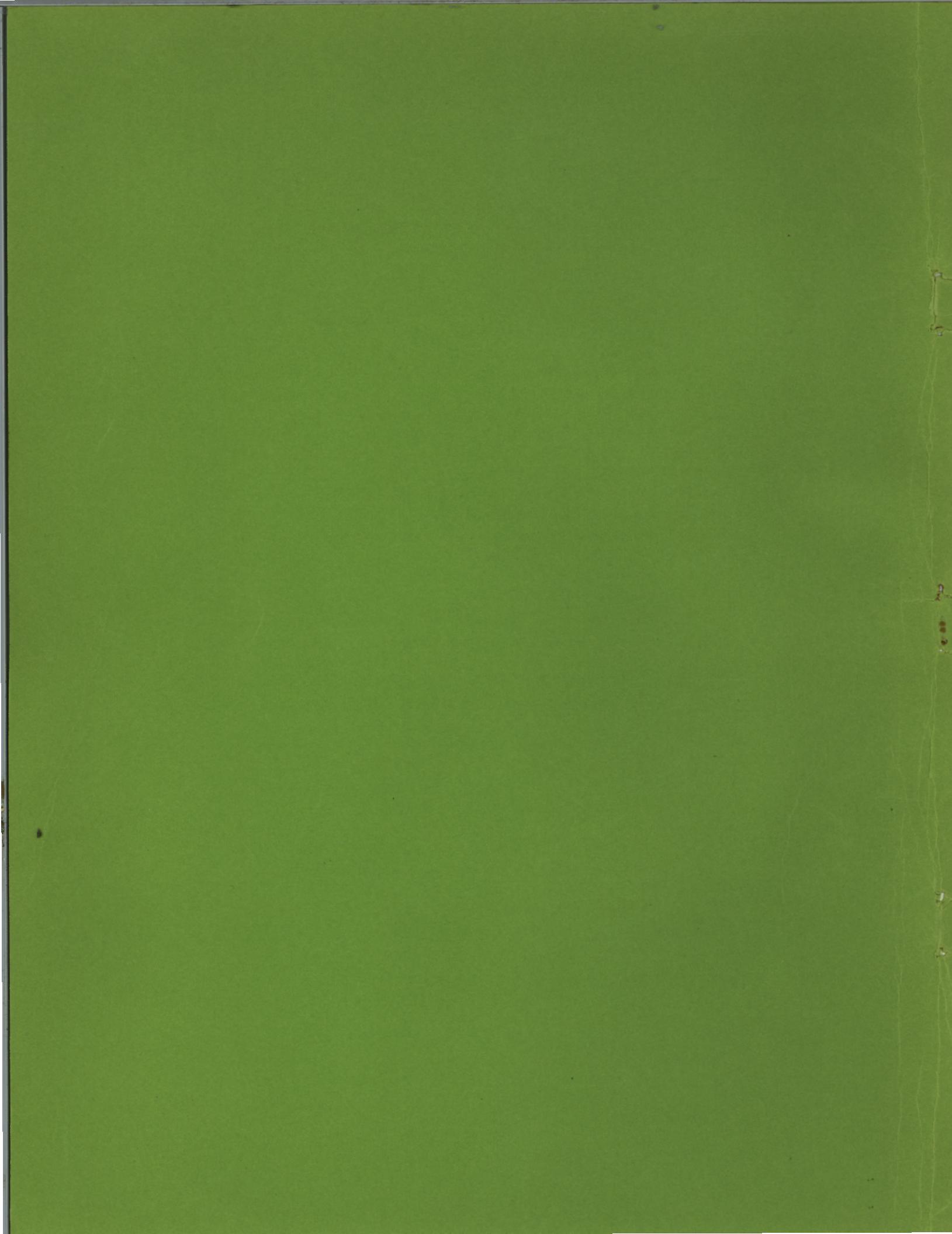
MEMBERS OF COMMITTEE PRESENT:

Senator Laurence S. Weiss, Chairman
Senator Walter Rand
Senator John H. Ewing
Senator Walter E. Foran
Senator John P. Gallagher

ALSO PRESENT:

Allan Parry, Analyst
Office of Legislative Services
Aide, Senate Revenue, Finance and
Appropriations Committee

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SENATE CONCURRENT RESOLUTION No. 3027

STATE OF NEW JERSEY

INTRODUCED JUNE 16, 1983

By Senator WEISS

Referred to Committee on Revenue, Finance and Appropriations

A CONCURRENT RESOLUTION proposing to amend Article VIII,
Section II, paragraph 3 of the Constitution of the State of New
Jersey.

- 1 BE IT RESOLVED by the Senate of the State of New Jersey (the
- 2 General Assembly concurring):
 - 1 The following proposed amendment to the Constitution of the
 - 2 State of New Jersey is hereby agreed to:

PROPOSED AMENDMENT

3 Amend Article VIII, Section II, paragraph 3 is amended to read
4 as follows:

5 3. The Legislature shall not, in any manner, create in any fiscal
6 year a debt or debts, liability or liabilities of the State, which
7 together with any previous debts or liabilities shall exceed at any
8 time one per centum of the total amount appropriated by the
9 general appropriation law for that fiscal year, unless the same
10 shall be authorized by a law for some single object or work
11 distinctly specified therein. Regardless of any limitation relating
12 to taxation in this Constitution, such law shall provide the ways
13 and means, exclusive of loans, to pay the interest of such debt or
14 liability as it falls due, and also to pay and discharge the principle
15 thereof within thirty-five years from the time it is contracted; and
16 the law shall not be repealed until such debt or liability and the
17 interest thereon are fully paid and discharged.

18 [No] Except as hereinafter provided, no such law shall take
19 effect until it shall have been submitted to the people at a general
20 election and approved by a majority of the legally qualified voters

EXPLANATION—Matter enclosed in bold-faced brackets [thus] in the above bill
is not enacted and is intended to be omitted in the law.
Matter printed in italics thus is new matter.

21 of the State voting thereon. *No voter approval shall be required*
22 *for any such law authorizing the creation of a debt or debts in a*
23 *specified amount or an amount to be determined in accordance with*
24 *such law for the refinancing of all or a portion of any outstanding*
25 *debts or liabilities of the State heretofore or hereafter created, so*
26 *long as such law shall require that the refinancing provide a debt*
27 *service savings determined in a manner to be provided in such law*
28 *and that the proceeds of such debt or debts and any investment*
29 *income therefrom shall be applied to the payment of the principal*
30 *of, any redemption premium on, and interest due and to become due*
31 *on such debts or liabilities being refinanced on or prior to the re-*
32 *demption date or maturity date thereof, together with the costs*
33 *associated with such refinancing.* All money to be raised by the
34 authority of such law shall be applied only to the specific object
35 stated therein, and to the payment of the debt thereby created. This
36 paragraph shall not be construed to refer to any money that has
37 been or may be deposited with this State by the government of the
38 United States. Nor shall anything in this paragraph contained
39 apply to the creation of any debts or liabilities for purposes of war,
40 or to repel invasion, or to suppress insurrection or to meet an
41 emergency caused by disaster or act of God.

1 2. When this proposed amendment to the Constitution is finally
2 agreed to, pursuant to Article IX, paragraph 1 of the Constitution,
3 it shall be submitted to the people at the next general election
4 occurring more than three months after such final agreement and
5 shall be published at least once in at least one newspaper of each
6 county designated by the President of the Senate and the Speaker
7 of the General Assembly and the Secretary of State, not less than
8 three months prior to said general election.

1 3. This proposed amendment to the Constitution shall be sub-
2 mitted to the people at said election in the following manner and
3 form:

4 There shall be printed on each official ballot to be used at such
5 general election, the following:

6 a. In every municipality in which voting machines are not used,
7 a legend which shall immediately precede the question, as follows:

8 If you favor the proposition printed below make a cross (X),
9 plus (+), or check (✓) in the square opposite the word "Yes."

10 If you are opposed thereto make a cross (X), plus (+) or
11 check (✓) in the square opposite the word "No."

12 b. In every municipality, the following question:

		BOND REFINANCING Do you approve the amendment to Article VIII, Section II, paragraph 3 of the Constitution, which authorizes the Legislature to enact laws, without further approval by the voters, authorizing the creation of a debt or debts for the refinancing of all or a portion of any current or future outstanding debt or liability of the State previously approved by the voters, so long as such laws shall require that the refinancing provide a debt service savings?
	No.	INTERPRETIVE STATEMENT The approval of this amendment would allow the Legislature to authorize the refinancing of State indebtedness without further voter approval in those cases where a debt service savings results. The amendment would allow the Legislature to take advantage of refinancing possibilities in those cases in which the State would realize a savings from the refinancing of a bond issue previously authorized by the voters.

STATEMENT

The purpose of this constitutional amendment is to grant greater flexibility to the Legislature in refinancing State bond issues previously approved by the voters. Currently, the New Jersey Constitution provides that any creation of State indebtedness must be approved by the voters. There is no specific provision which allows the Legislature to authorize a refinancing of State bond issues without voter approval, even if the refinancing were to reduce the amount of the State's debt service payments in the annual budget. This constitutional amendment would allow the Legislature to authorize refinancing without voter approval only in those cases where a debt service savings to the State results. Because refinancing involves the creation of new debt replacing old debt, the New Jersey Constitution must be amended to specifically authorize the Legislature to authorize the debt in cases where refinancing would yield a debt service savings.

This constitutional amendment would not allow the creation of new debt for projects which have not been authorized by the voters. It only allows for refinancing existing debt in those cases in which a debt service savings would be realized by the State.

This constitutional amendment would allow the Legislature to authorize actions which would facilitate greater financial flexibility without otherwise affecting the constitutional provisions which require the voters to approve all bonded indebtedness. The current wording of the constitution effectively precludes the State from taking advantage of refinancing possibilities which are financially advantageous to New Jersey.

I N D E X

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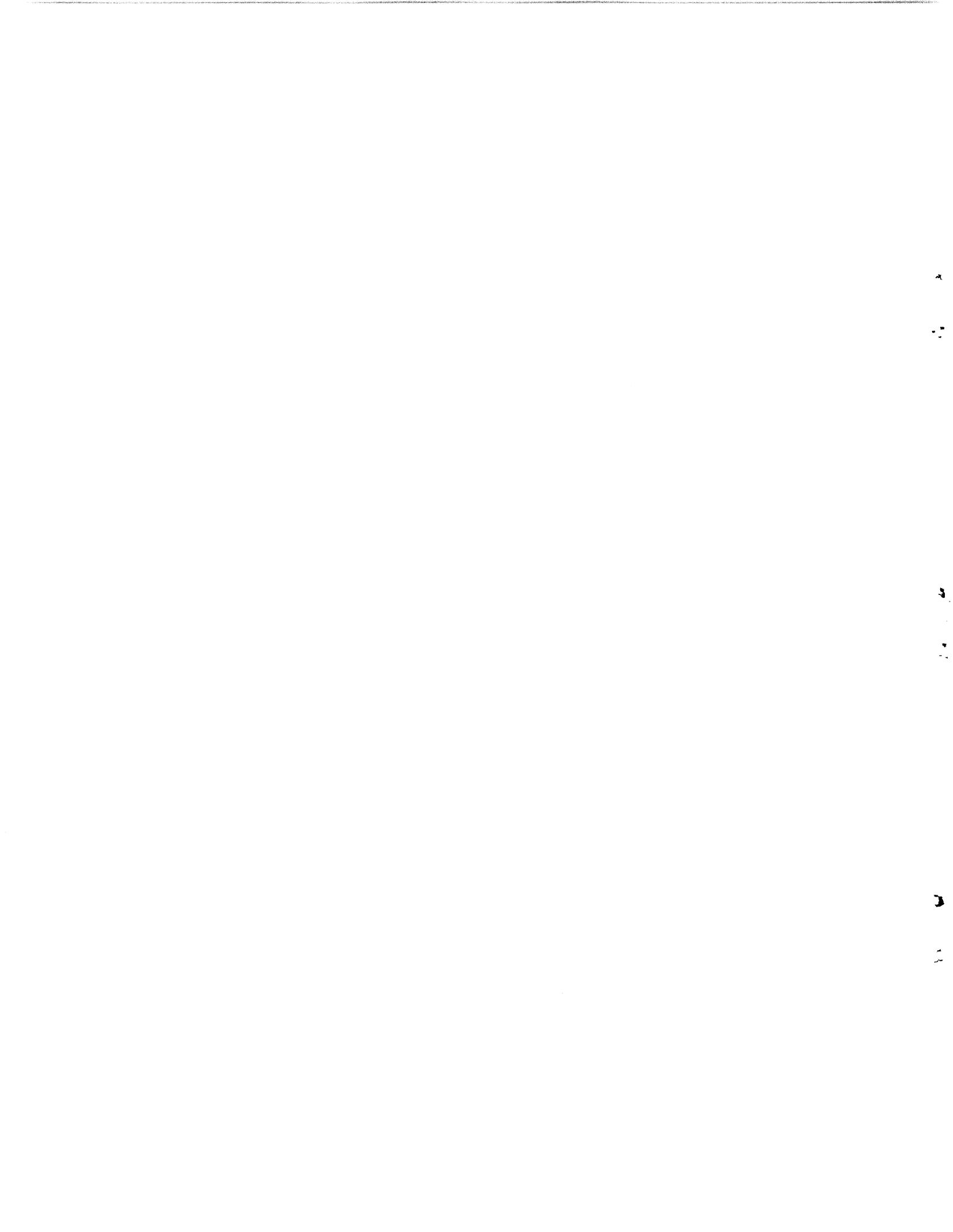
Douglas R. Forrester
Assistant Treasurer
State of New Jersey
Department of the Treasury

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Elizabeth B. Felker
Assistant Treasurer
State of New Jersey
Department of the Treasury

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mjz: 1-37



SENATOR LAURENCE S. WEISS (Chairman): Good morning, ladies and gentlemen. This public hearing is being held today to satisfy the provisions of Article IX, Paragraph 1 of the Constitution of the State of New Jersey, and Rule 166 of the Senate, which require that a public hearing be held on any proposed amendment to the State Constitution. The subject of today's hearing is Senate Concurrent Resolution No. 3027, a proposal to amend Article VIII, Section II, Paragraph 3 of the Constitution of the State of New Jersey. If approved by the Legislature and the electorate, this proposed amendment would permit the Legislature to authorize the refinancing of the State debt without further approval by the voters, to refinance all or a portion of the outstanding State debt, if such refinancing provides a debt service savings.

Before I introduce the first witness, I would like to introduce my colleagues, Senator Walter Foran, Senator John Gallagher, Mr. Allan Parry, a staff specialist, and Rosemary Kramer, aide to Senator Foran. The first witness this morning is Mr. Douglas Forrester, who is an Assistant State Treasurer. Is that right?

MR. FORRESTER: Yes, sir.

SENATOR WEISS: Mr. Forrester, you're on.

D O U G L A S R. F O R R E S T E R: Mr. Chairman, members of the Committee, thank you very much. I am Doug Forrester, Assistant Treasurer. Assistant Treasurer Liz Felker, who is sitting with me, and I are here on behalf of the Treasurer to present testimony on the Concurrent Resolutions SCR-3027 and ACR-3044. These are identical resolutions proposing the bond constitutional amendment as Senator Weiss has read it.

Let me first say that we also have with us Mr. Robert Fowler from L. F. Rothschild of New York, an investment banker, and Mr. Edward DeSeve and Kim Young from the Merrill Lynch White Weld Capital Markets Group. We have asked them to come down to join us this morning in our testimony, with the thought that there may be technical questions about this refinancing proposal which you may wish to ask, which may be better answered by those individuals who have participated in refunding proposals across the country.

The first thing I should say about the constitutional amendment we are proposing is that we believe it will offer the greatest flexibility to the State of New Jersey in financial matters, without jeopardizing the constitutional protection that the citizens of the State have with regard to

indebtedness. The basic proposal is to allow the voters to approve a mechanism which would be put into place as a constitutional amendment, which would allow the Legislature to approve refinancing or refunding proposals made by the Administration.

Currently, as you are aware, any indebtedness which is made by the State of New Jersey in terms of large bonds has to be approved by the voters. This voter approval process is certainly appropriate for bond projects. However, it does not allow for the refinancing of bonds without further voter approval, even though there are no additional projects being funded. Given the fact that the market has developed over the past few years in such a way as to have interest rates which have fluctuated dramatically, we have found ourselves in a position of desiring to refinance or refund certain bonds. Currently, the Constitution does not allow us to do this without going directly to the voters and getting voter approval for a specific refinancing proposal.

I'm sure you can appreciate that the constitutional impediment here is not something which is, we feel, in the public interest. The reason why is because the purpose of the Constitution at this point in time is to ensure that the level of indebtedness for the State not be increased without the voters' approving it. A refinancing proposal is something which is predicated on different grounds. It is based upon the proposal that we are not creating entirely new debt, except in the technical sense. The debt which will be created to refund the existing debt is something which we believe is entirely consistent with the intent of the Constitution in terms of the limitation on indebtedness.

We would like, through this proposal, to allow the Legislature to approve a refinancing proposal, and then have that be carried out by the Department of the Treasury. We are confident that the savings, which I believe Assistant Treasurer Felker will elaborate on, warrant this constitutional change. We are also confident that there will be no harm done to the constitutional intent in terms of giving undue latitude to the Administration. The proposal is something which we believe the Legislature will participate in intimately. Any proposal which is advanced for refinancing will have to be approved by the Legislature before it can be carried out.

What I would like to do now is ask Assistant Treasurer Felker to describe the mechanics of this proposal, and to explain in some detail how it a refinancing would work out.

SENATOR WEISS: Before you do that, Doug, there is a question by Senator Foran.

SENATOR FORAN: Doug, a few years back when Cliff Goldman was the Treasurer of this State, they recalled a set of bonds from the Meadowlands Complex at a certain high figure, and reissued them at a lower figure because the bond market had dropped off substantially. The fact that it was a separate authority, would that have anything to do with the constitutional question, or was he in violation of the Constitution, or was he within his rights to do that with a special authority? I just want to get that cleared up before we start.

MR. FORRESTER: I think you are correct in assuming the relationship we had with the Sports Authority with regard to that financing was decisive in terms of allowing that to be done. Clearly the Treasurer would not be able to proceed in an unconstitutional manner. If I recall correctly, and perhaps someone would wish to correct me, our responsibility in that refinancing was not the responsibility of full faith and credit of the State, and that is what is decisive here.

We are talking in this proposal about general obligation bonds which have the full faith and credit of the State of New Jersey behind them. That is what requires voter approval.

SENATOR FORAN: Later on then I am going to take umbrage with what you just stated. It seems to me I recall that this full faith in the State of New Jersey was put behind the bonds of the Sports Authority by a special piece of legislation, in order to allow a lot of New Jersey bankers to get into it. I think that was one of the problems we had with the New York banking people, where they would not come into that size money. I just wanted to clarify the record with you on the constitutionality of what Goldman did a couple of years ago, because he saved an awful lot of money for the taxpayers by doing what he did, as the bond market had dropped off considerably. I only bring that up because it was a special authority, as compared to the debt run by, say, your office, the Treasurer's office of the State. I think it is a little bit different, so I just wanted to clarify that to see whether or not that is true. But the full State backing of the

Sports Authority bonds was done by the Legislature, because it was the one way we could get it done.

MR. FORRESTER: I would like to ask Assistant Treasurer Felker to comment on that if I may.

E L I Z A B E T H B. F E L K E R: To analyze that question in a different fashion the first question to ask is, by what authority does an entity achieve the ability to issue bonds, and the authority that the Sports Authority had to issue bonds derived from the Legislature. The Legislature agreed to put the State's guarantee behind that bond; that is correct. However, the dollar amount of the debt the Sports Authority could issue was given to it by the Legislature.

The people give the State the dollar amount of debt that it can issue for full faith and credit general obligation bonds of the State in a constitutional referendum. That is what Section VIII of the Constitution does. It says that no debt of the State may be created except by a referendum. That has a specific dollar limit. Cliff Goldman did not do anything in violation of that, because he was not issuing those kinds of bonds.

SENATOR FORAN: I'm sure he didn't, but for the record of this hearing I wanted to clarify that there are a couple of different types of bonding within the State, and special authorities have been given the authority by the Legislature, even though they do have the full faith of the State behind them. That is a little bit different from what we are talking about under this bill.

MRS. FELKER: That's true.

SENATOR FORAN: I wanted to clarify it, that's all.

MRS. FELKER: Those are not going to be rated as highly as our full faith and credit bonds either, for that reason.

SENATOR FORAN: I just wanted to clarify the record, because we are dealing with two different types of financing here, and I wanted to clear the record before we got into further detail of what we are talking about this morning under this concurrent resolution.

MR. FORRESTER: I think, Senator, if I may just comment further, it is important to distinguish between the kind of backing. The backing that the voters give is that which is required by the Constitution. It is true that the legislation which was passed with regard to the Sports Authority

is a little stronger than the moral obligation. However, it does not attain quite the status that the general obligation bond does.

SENATOR WEISS: Thank you, Senator Foran. Senator Rand?

SENATOR RAND: Thank you, Mr. Chairman. I remember the Meadowlands very well, but I also remember another bond that was refinanced. I think the New Jersey Health Care Facilities -- wasn't that a refinanced--

MRS. FELKER: You are thinking of the University of Medicine and Dentistry bonds that have been issued by the New Jersey Health Care Facilities Finance Authority. They were refunded by State general obligation bonds.

SENATOR RAND: That was done by the Treasurer, am I correct?

MRS. FELKER: That's right, but that is not the same thing as we are talking about now.

SENATOR RAND: Yes, but it was a reduction in the rate at that time.

MRS. FELKER: In cost. The motivations for both the Sports Authority refinancing and the one you are speaking of are identical to our motivations in looking to refinance the State's general obligation bonds, to lower the cost of servicing the debt on those bonds.

SENATOR RAND: Are you saying that the actions taken by the State Treasurer at that time were not in conformity with what the law should have done?

MRS. FELKER: Not at all, not at all. But, we could not go and refinance the bonds that were sold to refinance the Health Care Authority's bonds. We issued State general obligation bonds, and the ability to refinance them is quite limited. Maybe you would like me to discuss what we can do today, and what we can't do, so you can understand why we need to get some additional flexibility.

SENATOR WEISS: Liz, after the next question would you do that please. I have one question waiting with Senator Gallagher.

SENATOR GALLAGHER: Thank you, Mr. Chairman. First of all, Doug and Liz, did we not have to go to the people in order to get permission to put the State guarantee behind the Parkway bonds, the senior bonds?

MR. FORRESTER: Yes, I believe that is correct.

SENATOR GALLAGHER: Do you have to go to the people all the time before you put a State guarantee behind any of those authority bonds, such as

the Sports Authority bond? Because, they are Triple "A" bonds; they are State guaranteed. It is not just a moral obligation of the State; there is a State guarantee behind those bonds, which they got in order to refinance them from the 7.5% of '09 to get a lower rate. Did we go to the people at that time? I thought we did, to get their permission for the State guarantee.

MRS. FELKER: I was not here at the time, so I do not have any personal knowledge of that, but I believe that is the case. If you are going to guarantee or dedicate a tax to a specific purpose, it has to be constitutional. With the Highway Authority bonds, we guarantee payment on -- oh, there is about \$43 million outstanding on those bonds and the Sports Authority bonds. There are other things called moral obligations which are not submitted to the voters; they are acts of the Legislature.

SENATOR GALLAGHER: A moral obligation -- that's what that is. But, with a State guarantee, you have to go to the people in order to get the approval?

MRS. FELKER: Depending on what that referendum language was. It would depend on whether they could exceed the amount of indebtedness in a refinancing to be greater than the amount of indebtedness they had originally. If it set a ceiling on it and they were still under that ceiling, they would be all right.

SENATOR GALLAGHER: We can check on the Sports Authority, but I think originally they gave the moral pledge and then they went for the State guarantee. I think they did go to the people in order to put that there. On the Medicine and Dentistry, did you go to the people for permission to float bonds?

MRS. FELKER: There had to have been a referendum in 1977 in order to authorize those medical facilities' bonds.

SENATOR GALLAGHER: Okay, so you did go to the people.

MRS. FELKER: Sure.

SENATOR GALLAGHER: So, we did comply with all of the constitutional requirements.

MR. FORRESTER: It would seem so, yes.

SENATOR GALLAGHER: Okay.

MR. FORRESTER: I do not think there is any question but that we did comply with the constitutional requirements.

SENATOR GALLAGHER: Okay. I have other questions, but I will wait until they testify. (Senator Gallagher apparently referring to future witnesses.) I have a whole list of them.

SENATOR WEISS: On the Sports Authority, when those bonds were floated originally the State was behind them as the guarantor, and we did lose our Triple "A" rating for awhile. I don't recall whether it was one year or two years, but we did lose it, and that was the only time we lost it since 1956. After that happened, I guess they saw the light and they just got their moral obligation behind it and the State was no longer the guarantor on the bonds. But, we did get our rating back after that.

MR. FORRESTER: Senator, I'm not sure that there is a relationship between the Sports Authority and when the State lost its rating.

SENATOR WEISS: Well, there is in only one aspect, and that is that if the State has other than a moral obligation, a stronger obligation, then certainly it would have affected the State rating, the Triple "A" rating.

MRS. FELKER: Those contingent liabilities do-- (Witness interrupted by workman drilling wall of room next door.)

SENATOR GALLAGHER: That is not true Larry.

SENATOR WEISS: What is not true?

SENATOR GALLAGHER: What you just said. It had nothing to do with the rating, the moral pledge of the State funds. It has to do with the ability of the State and how Moody's is going to have to look at the State at that time.

SENATOR WEISS: Well, that may be, but they were looking at it at that time from the point of view that we should not have used the full force in effect in the Constitution to guarantee the bonds.

SENATOR GALLAGHER: But, at that same time they downgraded the State guaranteed bonds at the Parkway too. As the State was affected -- every state guarantee was affected.

SENATOR WEISS: Well, yes, it affects everything, but the trigger in the thing was the bonds up at the Sports Complex. That is as I recall. I think Senator Rand knows a little more about it. He was here, and I think voted on some issue that had to do with that, didn't you, Senator Rand?

SENATOR RAND: Well, they put the full faith and credit of the State behind those bonds. I questioned them at that time, because I did not think we should put the full faith and credit of the State behind the bonds. But, Goldman was a little more persuasive, and--

SENATOR GALLAGHER: That was refinancing.

SENATOR RAND: At the refinancing, and they did put the full faith and credit of the State behind it.

SENATOR GALLAGHER: But, that was in 1977.

SENATOR RAND: Do you remember that, Walter, in 1977?

SENATOR FORAN: Yes.

SENATOR GALLAGHER: Yes, 1977-78, not when they started in 1972-73.

SENATOR RAND: No, 1977 it was, 1977 or 1978, right in there.

SENATOR GALLAGHER: But, they were then guaranteeing a sure bet at that point.

SENATOR RAND: Yes.

SENATOR GALLAGHER: They were making a lot of money.

SENATOR RAND: They saved about, if I remember correctly, \$60 million to \$80 million. Am I right on that? (no response)

SENATOR GALLAGHER: It was a lot of money.

SENATOR EWING: Tremendous.

SENATOR GALLAGHER: Now that we all know what we are talking about, we'll go back to square one.

SENATOR WEISS: Liz, would you explain what you started to explain?

MRS. FELKER: Surely. Let me try to put it in a framework for you, what we can now do. When we set up a bond sale, we have a choice as to the length of the longest maturity and the shortest maturity of the bonds, how the maturity structure is set up. We have a choice as to whether to make those bonds callable or not, and that choice is really a question of how much flexibility are we able to gain without costing ourselves more than we care to have it cost in the interest rate. If you wanted to have all of your bonds callable, the market would charge you a high premium for that because bondholders would not be able to keep their bonds very long. They would be afraid you would call them away. If you have no bonds callable, you have no chance to take advantage of lower interest rates.

What has been happening here in the State of New Jersey with general obligation bonds since around 1981, is that our bonds issued from then on have been callable, but not for ten years. So, all those serial bonds maturing for the first nine years of an issue have been noncallable; the remainder are callable. After the tenth year, and for the first five years of that call period, they have a premium attached, so you have to pay

more than 100% of the principal to get them back. This means that when we issued bonds in 1981 and 1982 at double digit interest rates -- and we have three hundred million in outstanding double digit interest rates -- we have no way to do anything about that interest cost, until they are callable. By the time they are callable, half of them, or more, will be retired. So, the question presents itself to us in Treasury, what can we do to make up for the very high cost we are forced to pay on these bonds we have already sold, now that interest rates have gone lower? We have bonds at 12.1% and 11.6%. The last series that we issued in April was at 7.8% on the average. So, we could do a great deal better if we were to issue all those bonds all over again today, but we cannot do that.

Having analyzed all the alternatives, we decided to pursue this avenue, this proposal that you are faced with today, and that is to give us the authority to do today what we would otherwise have to wait until 1991 or 1992 to do, to provide for the refunding of those bonds at lower interest rates. That is what this is all about. We cannot do that today under the bond acts, because the bond acts all have a provision, which they have because of the way the Constitution is worded, that any refunding that is done under that bond act cannot have a greater principal amount than the original bond act provided. If we sold \$100 million worth of bonds under a bond act, and \$50 million worth of them are still left outstanding and we want to refund them, we can only sell \$50 million of refunding bonds.

To take advantage of the lower interest rates by providing for advance refunding of those bonds that become callable, we must sell a larger principal amount. This is necessary in order to achieve the rather complicated structure which permits us to get at the savings earlier. Because the Constitution clearly says that the people must vote for the exact principal amount of the debt outstanding, we are foreclosed from doing that. Therefore, we determined that we needed to ask the people for permission to issue refunding bonds, and have that be distinguished from the permission to issue bonds for specific purposes, such as highway construction such as Green Acres, or such as the hospital and medical facilities, or any other of the various bond acts that have been passed over the years.

The specific purpose of these bonds is for refunding. It is not for new money for new construction. There are two possible ways to do that. You could go to the ballot and say, "Here is a bond act, and these are going

to be called refunding bonds of 1983. They will be used to refund certain old series." That is a very complex piece of legislation, and it would have to come, again and again, if there were refunding opportunities in the future that we did not contemplate today. The simplest and cleanest solution we felt -- and we developed this conclusion with the aid of counsel from both the Attorney General's Office and our outside counsel -- was to say, "Let us distinguish refunding bonds from general obligation bonds for public purposes, and we will except them, get them out from under that limitation of needing to approve the exact dollar amount. Let's let the Legislature approve refunding of outstanding bonds, with the proviso that they will only do so when there is a debt service savings." Now, that is an explanation of the framework within which this proposal has been developed.

MR. FORRESTER: If I may just add a comment here, I think it would also be worthwhile to note that the consideration of the flexibility of this refinancing is something that, although technically it is possible to go year after year to the voters for a refinancing proposal, I think the nature of financial possibility is such that it is not prudent to have to be limited to a date in November for the approval of such a refinancing scheme.

SENATOR WEISS: Doug, before you go on, I would like to introduce two of the members who came in, and they are Senator Walter Rand on my left, and Senator John Ewing on my right, and Mr. Gerald Silliphant, the Legislative Budget Officer, on my far left, not normally to the left of me, but he is on my left.

I have two questions at the moment, one by Senator Gallagher, and then one by Senator Foran, in that order.

SENATOR GALLAGHER: Thank you, Mr. Chairman. Doug, all the bonds that we have out that are presently over what the rate might be if you went to market today, are they subject to a ten-year call?

MR. FORRESTER: I believe most all of them are; I cannot say for sure if all of them are.

MRS. FELKER: Yes, those issues were sold with a ten-year call.

SENATOR GALLAGHER: Now, the longest maturity on those bonds, what were they, twenty, twenty-five year bonds?

MR. FORRESTER: The longest maturity I think would be twenty-five. Is that correct?

MRS. FELKER: They were both twenty year bonds, or twenty-one years.

SENATOR GALLAGHER: Twenty or twenty-one years?

MRS. FELKER: Yes.

SENATOR GALLAGHER: So, you are talking about refunding just ten years?

MRS. FELKER: We are talking about refunding either two hundred and eighty-five million of the original three hundred million, or only those bonds which are callable, depending on which generates the best savings. That is partly a function of the maturity structure that you put on the refunding bonds.

SENATOR GALLAGHER: Why would you go out to refund the ten years that you are locked into?

MRS. FELKER: Refunding the first ones? Only if you wanted to slightly rearrange the maturities. Normally, you would achieve no savings at all. You don't have to do that. You are really only trying to refund those longer term bonds.

SENATOR GALLAGHER: You would be parlaying the front end of it in order to justify the back end of it.

MRS. FELKER: No, you don't even need to touch the front end, but you could. You would have that opportunity.

SENATOR GALLAGHER: Okay, that is what I'm saying.

MRS. FELKER: The way in which you would judge whether to do that, in addition you would do a number of modelings to see what kind of structure would achieve what kind of savings. Then you would look to see what that did to your total debt picture -- to the average maturity of your total debt. You wouldn't want to do something that would suddenly make our long-term debt have a longer average maturity. That would be a mistake.

SENATOR GALLAGHER: That is what I am trying to get to, too.

MRS. FELKER: Right.

SENATOR GALLAGHER: Are you talking about expending the maturity in the debt obligation of the State through a refunding process?

MRS. FELKER: No, we are not.

SENATOR GALLAGHER: Are you talking about refunding an '80 issue for the same--

MRS. FELKER: You refund an issue that was sold for twenty years with a nineteen year issue; it is done a year later.

SENATOR GALLAGHER: If you did it a year later. But then you would be talking of possibly refunding the nine years for which you are still obligated to pay the higher rate of interest, because the bonds are not callable until then.

MRS. FELKER: It is possible to do that. It is not necessarily advisable. That is not where you are going to realize-- The major savings are going to come from those callable bonds.

SENATOR GALLAGHER: Okay. The cost to the State on a competitive bid for the bonding, what does that run on \$100 million bond issue?

MRS. FELKER: Well, on \$150 million, just the transaction cost -- we'd have \$100,000 or \$200,000 at the most.

SENATOR GALLAGHER: Okay. The costs that are refinanced?

MRS. FELKER: It shouldn't be very different, it's the same general process.

SENATOR GALLAGHER: It should be about the same.

MRS. FELKER: You might have extra computer expenses.

SENATOR GALLAGHER: We're talking about refunding strictly for the financial benefit, the financial savings?

MRS. FELKER: That's right.

SENATOR GALLAGHER: Refinancing it so that we can get a lower cost overall, not only the debt service, but also the cost of the refinancing itself.

MRS. FELKER: That has to be taken into account.

SENATOR GALLAGHER: We are not talking about any restrictive covenants or anything else that might be in, and there may not be any in the general obligation issues of the State, as there are in some of the revenue bonds of the authorities.

MRS. FELKER: The proposed amendments clearly state that this shall be done when there is a debt service saving. That would not preclude you from doing something else in addition.

SENATOR WEISS: I think that is in there. The indication is other than debt service too, as I read it, but any other obligations other than the interest obligation would trigger a refinancing.

MRS. FELKER: Let me give you an example of something you could do. There are appropriations in these bond acts from different funds. I know you are aware of different taxes providing a source of debt service for

different kinds of bonds. For instance, the sales tax backs most of the bonds; certain bonds are backed by the corporation business tax, for instance, the Green Acres bond. The transportation bonds have been backed by appropriations of motor fuel revenues. I know Senator Rand is aware of that. You could, in a refinancing, appropriate a different source of revenue. That is the kind of thing that could be done. That is not the reason for this, but refundings are sometimes done to accomplish things of that kind. We have not been trying to do anything like that, but this would permit the Legislature to consider those other kinds of options.

SENATOR GALLAGHER: Well, I agree with the concept of trying to find a way to save money when you have to go out to do something at a particular time and pay whatever the market demands, but I think we ought to be extremely cautious in broadening this thing because this is one area where the public's interest always has to be protected, because the Constitution provides that the public is going to be the final word as far as debt is concerned. I would be a little bit concerned about having these things permissible because of some restricting covenants, etc. I would not want to see some people turning in our bonds so they could make money on the outside.

Now, what are the arbitrage regulations today, because you are talking about putting these refunding things into escrow accounts, aren't you?

MRS. FELKER: That's right. The proceeds of the refunding bonds would be used to purchase U.S. government securities. These are a specific type of U.S. government securities which the Treasury Department in Washington issues, which enable you to exactly match the maturities of those securities that you buy to your needs to repay the debt on your existing bonds. The arbitrage regulations will not permit you to make any money in that transaction. Your cost of issuance and your debt service have to be no less than the yield on the bonds to wash.

SENATOR GALLAGHER: Didn't they arbitrage an eighth of a point?

MRS. FELKER: Do you mean in terms of the allowable expenses?

SENATOR GALLAGHER: As far as what you can go out for over and above what your new situation is going to be.

MRS. FELKER: There are some very new regulations on this, and I think I would be more comfortable if I called on one of our experts. Would you object to that?

SENATOR GALLAGHER: Well, I think we can get into that later, you know. We can get into that later, because I would like to find out exactly what we are talking about, the period of time, and what we can do as far as savings like your 1210's. I think you have some 1210's out.

MRS. FELKER: Yes, that's right.

SENATOR GALLAGHER: What are you going to do about those?

MRS. FELKER: Oh, do you mean in terms of how many statements we can generate?

SENATOR GALLAGHER: Yes, when we get there. We will get there later.

SENATOR WEISS: Yes, we'll get there, but I have other questions from other people, and then probably we will touch on other parts of this issue. We will come back to this when you have your experts, and we'll have them on. Senator Foran, I believe you were next.

SENATOR FORAN: Thank you, Mr. Chairman. I would like to play the devil's advocate for a minute. I buy some bonds, State educational facility, or whatever, at 12% or 10%, or so forth. The bond market goes down two or three points or whatever. Do you have the authority then, if this passes, to recall those bonds and reissue bonds at the lower rate, saving the taxpayers of the State of New Jersey an awful lot of money, as was done in the Sports Authority case?

MR. FORRESTER: Senator, may I just make an observation. We are not really talking about calling in those bonds immediately, and perhaps if that is affecting your question that should be made clear.

SENATOR FORAN: I would like to know what happens to the guy who buys the bonds. I am playing the devil's advocate now. If I bought some bonds at 12%, we'll say, and under this proposal you can reissue refunding bonds, do I maintain the 12%, or do I get it at the new rate?

MR. FORRESTER: That is why these securities are purchased, as Assistant Treasurer Felker mentioned. These are purchased in order to provide for that flow of payment to you as that bondholder who made the purchase at 12%, and that is continued. That person continues to receive the payments according to the original schedule and terms.

MRS. FELKER: Nothing would happen to you, other than two things. If you owned that bond at 12.1%, two things would happen to you. One is, your credit support would change. You would no longer be secured by the

State of New Jersey; you would be secured by the U.S. government. That would be good for you, because it gives you-- Although some might feel that we are better than the Federal government, they still print the money. So, they become--

SENATOR FORAN: That is very questionable.

MRS. FELKER: They become your security. We never forget who was here first, right? The other thing that happens to you is that you now know that you will be called out at the first call date, which in the case of the 1210's will be in November, 1991. You will not have the benefit of the rest of the ten years off-- If you bought the longest bond that was issued at that time, you would not be able to get that 12.1% after that time. That is the risk you took, though, when you bought the bond, because it said in fine print, "This bond is callable after 1991."

SENATOR FORAN: It only becomes a risk if this passes.

MRS. FELKER: That's true. Well, no, we could still call your bond down in 1991.

SENATOR FORAN: You can call it anytime after ten years?

MRS. FELKER: That's right, but you get an extra 3% premium at the time though.

SENATOR FORAN: The point I'm making is the fact that we have gone out in the marketplace when the market has been high -- you said double digit interest rates and so forth -- and somebody buys a bond in good faith as an investment. And, all of a sudden, we're now saying that is not going to be such a good investment because we are going to revamp the backing of the bonds to treasury notes, or whatever, and you are going to be subject to, say, an early recall, or whatever. As a devil's advocate, what is going to happen on the bond market to people or institutions who buy our bonds? We change the rules in the middle of the game.

MRS. FELKER: We haven't changed anything, because we are only acting under the original rules. The original rules said, "Yes, you can call the bonds." We said to the market, "We are going to put a provision in these bonds that they are going to be callable at 103% of par in November, 1991," and we can make a decision to do that. We can make a decision today, or--

SENATOR FORAN: (interrupting) Well, I think you have covered it, because with this authority you can call them in early. That is what you are trying to say.

MRS. FELKER: Right. It is just a question of when we decide; it is not a question of when they are called.

SENATOR FORAN: Well, as I say, I was just trying to ascertain whether or not it was fair to the guy who puts his money out on bonds in the first place.

MRS. FELKER: I think that is a reasonable question. We do have concern about what our bondholders think and about the perception the market has.

MR. FORRESTER: You would not be subject to any greater uncertainty under our constitutional amendment than you are currently in terms of being a bondholder.

SENATOR FORAN: Thank you.

SENATOR WEISS: Thank you, Senator Foran. Senator Rand, do you have a question?

SENATOR RAND: Yes, thank you, Mr. Chairman. If I understand it then, under this proposal the bondholder is protected the same as under the other proposal. Is that correct? What is callable, is callable; what's not, is not. What interest is paid and what premium is paid will still be paid.

MR. FORRESTER: Yes.

SENATOR RAND: Okay, fine. When you refinance, in your new bonds, is there a callable period in those bonds?

MRS. FELKER: We would structure them in much the same way.

SENATOR RAND: Exactly the same way?

MRS. FELKER: Yes. So, you could do it to them too later on.

SENATOR RAND: In other words, you could then refinance and then put in a ten-year callable period for those new bonds?

MRS. FELKER: That's right.

SENATOR RAND: Okay, which brings me to my final question. If I am to understand the theory of this, if you are refinancing a bond issue of \$100 million and you paid off \$50 million, you could then refinance at \$100 million. Is that correct?

MRS. FELKER: No, you could only refinance what has not been paid off.

SENATOR RAND: Just the balance?

MRS. FELKER: That's right.

SENATOR RAND: Fine. So, you do not increase the debt at all; all you are trying to do is reduce the debt service.

MRS. FELKER: That is exactly right.

SENATOR RAND: Thank you very much, Mr. Chairman.

MR. FORRESTER: Senator, may I make a point of clarification here?

SENATOR WEISS: You will have to do it through the Chair, because I have a Committee up here that I have to contend with. Okay?

MR. FORRESTER: I understand.

SENATOR WEISS: So, don't preempt me.

MR. FORRESTER: I certainly wouldn't.

SENATOR WEISS: I will let you make your explanation after Senator Gallagher.

MR. FORRESTER: That's fine, thank you.

SENATOR WEISS: Senator Gallagher -- if you don't take a half hour.

SENATOR GALLAGHER: I'm not going to be a half hour; I just want to clarify one point. I gather you have never, ever called any bonds?

MRS. FELKER: We have never had the opportunity.

SENATOR GALLAGHER: And, the reason you never had the opportunity might be because you never put any issues out that were subject to call until maybe recently with the higher rates. How would you call them? Where would you get the money to call?

MRS. FELKER: Well, if we were not doing a refunding, there would be two ways you could do it. If we were not doing an advance refunding, we could just plain old refund them, and in 1991 you could take \$100 million of callable bonds, call them, and refinance them with another \$100 million.

SENATOR GALLAGHER: You're talking about refinancing?

MRS. FELKER: That's refinancing.

SENATOR GALLAGHER: So, without this, you really can't call the bonds, because you don't have the funds to do it, do you?

MRS. FELKER: No, we can do that under the Bond Act. You can take an equal amount.

SENATOR GALLAGHER: No, you have the legal right, but where would you get the money to do it?

MRS. FELKER: You would have to borrow it again.

SENATOR GALLAGHER: Okay. Well, that is what I am saying. You would have to borrow it again. So, you have callable bonds out there right now at a ten-year call, but you have no vehicle to get the funds to call unless this goes through?

MRS. FELKER: No, that is not true.

SENATOR GALLAGHER: Where would you get the funds? All of the bond issues that are approved by the voter at the present time are for specific projects, are they not?

MRS. FELKER: That's true.

SENATOR GALLAGHER: Where would you get the \$200 million to call those bonds?

MRS. FELKER: Every bond act has a provision in it that provides for refunding. It says that you can refund the bonds as long as your interest rate -- taking into consideration the call premium, if any, that is paid -- deals off no greater cost in debt service than you currently have. That is what they let you do. So, let's say it is 1991 and we have \$50 million in bonds that are callable in that year, and interest rates are enough lower that we could issue another \$50 million worth of bonds to pay off the first \$50 million and the call premium and still have the lower cost, we would be permitted to do that under the current Bond Act. That is exactly the problem though. We would have to wait until 1991 to do anything at all. What we are saying is that we think today's taxpayers should have the advantage of the lower interest rates, and not wait until the taxpayers of 1991.

SENATOR GALLAGHER: Oh, okay. So, you're saying that the present law permits you to put a new issue out to call those bonds?

MRS. FELKER: That's right.

SENATOR GALLAGHER: It does?

MRS. FELKER: It does, as long as it is not a greater principal amount.

SENATOR GALLAGHER: As long as it is not a greater principal amount than the remaining bonds?

MRS. FELKER: That is correct. The other way, of course, that you could call them--

SENATOR GALLAGHER: (interrupting) Or a higher cost?

MRS. FELKER: If the Legislature cared to appropriate money to call bonds with, it could certainly do that.

SENATOR GALLAGHER: Sure, I understand that one, but I would like to know where they are going to get it.

MRS. FELKER: Well, we'll worry about that in 1991.

SENATOR WEISS: Doug, you had an explanation for Senator Rand, I believe.

SENATOR RAND: No, I'm finished, Mr. Chairman.

SENATOR WEISS: No, Doug Forrester had something for you.

SENATOR RAND: Yes, okay.

MR. FORRESTER: Thank you, Mr. Chairman. I wanted to make sure there wasn't any uncertainty, Senator Rand, with regard to this issue of increased debt. Assistant Treasurer Felker did mention that, because of the way we are making the calculations in terms of interest rates, there will be more debt incurred in the refinancing in order to refinance the existing debt.

SENATOR RAND: Tell me why.

MR. FORRESTER: Well, the reason why is because, in order to set aside an amount of money in these government securities to adequately fund and pay off Senator Foran's bondholder that he referred to a few minutes ago--

SENATOR RAND: When it becomes callable. Senator Foran is the bondholder.

MR. FORRESTER: No, it isn't right. We have to set aside a larger amount of money than was originally incurred in terms of debt, because of the fact that it is being set aside and is earning money at a lower interest rate. We have to borrow a greater amount of principal in order to earn enough interest to pay off a bondholder who is being paid at a higher interest rate. Now, the important point here is that we are not talking about losing money. The whole purpose is to make sure that the State is in a position, over the long term, of gaining financially.

SENATOR RAND: Which could be twenty years.

MR. FORRESTER: Yes, however long the refund's period of time is.

SENATOR RAND: Which brings me back to the original question which I asked. If you have \$100 million bond issue and you have \$50 million paid off, I thought I heard you say originally that you could buy more bonds than the \$50 million. Then you said, "No, you have to buy the same amount of bonds."

MR. FORRESTER: I think perhaps the answer you received earlier was correct. Certainly, it was intended to be. I think we are talking about the fact that the whole purpose of the refinancing indebtedness is to go to pay off the existing debt, or rather to buy securities to ensure the payment of

that existing debt. We cannot borrow more money to use for different projects, or things like that.

SENATOR RAND: I understand, but you are selling more bonds so you can pay off over a long term?

MR. FORRESTER: Yes, there will be a greater amount in the refinanced debt than in the existing debt.

SENATOR RAND: Okay. Will that interfere with our Triple "A" bond rating when you increase that debt to a point?

MR. FORRESTER: Assistant Treasurer Felker had a discussion with one of the rating agencies recently, and perhaps it would be best to let her give an account of that conversation.

MRS. FELKER: To put that in context, when we take any action, whether it be authorized new bonds to sell existing authorized bonds or to refinance bonds, the rating agencies will look at our motivation in doing what we are doing, and at the results. They take into account always what the overall debt of the State is, but they are equally interested, if not more so, in the cost of servicing the debt. I had a specific discussion with one of the rating agencies to clear up this point for myself, because I had asked myself the same question. I said, "Gee, I wonder if you will consider this extra principal amount to be a liability to us." They said, "No, we understand that more debt will have to be issued in principal amount in order to achieve the principal and interest payment savings -- the debt service savings. We believe you should undertake these kinds of things in order to do a debt service savings, because it is good for you with respect to your fiscal management. So no, we do not count that against you. We adjust for it on our worksheets when we analyze your debt."

SENATOR RAND: Then, through you, Mr. Chairman, I am going to assume -- and I am in favor of this, by the way; I mean, this is a conception that I favor -- that you build your debt up, and I am going to assume that the financial agencies that rate us will understand as we build our debt up that we start at a high thing and begin to lower it over the years. Is that correct -- on our debt service?

MRS. FELKER: Yes, they will track the debt service, and they will track the outstanding debt, and they will do it by kind of debt.

SENATOR RAND: Because, that is the way the actuarial tables will show it, that you start at this point and work down. Am I correct?

MRS. FELKER: That is right.

SENATOR RAND: Thank you very much. Thank you, Mr. Chairman.

SENATOR WEISS: Thank you, Senator Rand. Senator Ewing?

SENATOR EWING: You stated that today you have the authority to issue bonds for the addition of new bonds to call in the ones that are called.

MRS. FELKER: That's true.

SENATOR EWING: What will the action in this bill do for you then?

MRS. FELKER: Under our current authority, we cannot take that action until the date that they are callable. And, the first date that any State bond at all is callable is in 1990.

SENATOR EWING: Oh, okay. I see.

MRS. FELKER: We don't see why we shouldn't give the current--

SENATOR EWING: (interrupting) All right. Now, in the statement here it says, "There is no specific provision which allows the Legislature to authorize a refinancing of State bond issues without voter approval, even if the refinancing were to reduce the amount..." Well, that is not true. There is authority, but you have to wait for the date. You have to wait for the callable date. This statement is actually not correct.

SENATOR GALLAGHER: Is that by the Constitution, or is that by her bond resolution?

MRS. FELKER: It is by the Bond Act.

SENATOR GALLAGHER: Oh, but that is not the Constitution.

SENATOR EWING: Do you agree with the statement on the bill?

SENATOR GALLAGHER: You're telling me what you can do with the Bond Act, but you have to get the funds and the permission for refinancing, and that's what this bill is going to do.

MRS. FELKER: The statement is correct in that it says there is no provision that says that the Legislature can take action to permit the refinancing.

MR. FORRESTER: The purpose of the statement is to communicate the fact that currently there is no mechanism in place to allow the Legislature to act unilaterally without voter approval.

SENATOR EWING: It doesn't say that here though.

MR. FORRESTER: Well--

SENATOR EWING: Well, read it. You read it to me.

MRS. FELKER: The issuing officials have that authority now; the Legislature has no authority to go and do anything additional.

SENATOR EWING: Well, I am just questioning that one sentence here, "There is no specific provision which allows the Legislature to authorize a refinancing of State bond issues without voter approval, even if the refinancing were to reduce the amount of the State's debt service payments in the annual budget." And yet, you are telling me you can do it but you have to wait for the callable date.

MR. FORRESTER: I do not believe that that requires legislative approval for that refinancing by the issuing officials.

MRS. FELKER: The only chance the Legislature has to get into that is when it originally votes on the Bond Act. Then it goes to the voters, then it is on the books, and then the rest of it is an executive activity.

SENATOR EWING: But, there are provisions now.

MR. FORRESTER: But, I think the technical distinction we are making here is that the refinancing Assistant Treasurer Felker is referring to, is one that is made by the issuing officials. I do not believe that the Legislature has to act in order for that to be done when the call date occurs.

MRS. FELKER: Let's say it a different way. That refinancing that you are talking about, at the call date, will have had voter approval. We're talking about a different thing, a refinancing without voter approval.

SENATOR EWING: Maybe it should state that in the statement, "refinancing without voter approval."

MRS. FELKER: It says that in the next sentence, I believe, sir.

SENATOR EWING: I am not talking about the next sentence; I'm talking about that statement.

SENATOR GALLAGHER: Larry, let's get one clarifying statement, I mean one clarifying question.

SENATOR EWING: I do not think it is very clear, frankly, for people who don't really know. You are involved in it everyday. Right?

SENATOR WEISS: Senator Gallagher?

SENATOR GALLAGHER: Let me just clarify one thing, and that is with regard to your ability to pay if you called those bonds in 1991. All right? You and the Legislature have to comply with the Constitution before you go out for a bond issue to pay for those, ten years after the ten-year call. You have to go to the people at the present time, do you not?

MRS. FELKER: No, we do not.

SENATOR GALLAGHER: Where do you have the authority, outside of if we came up in the Appropriations Committee with \$100 million in taxes to allow you to do it, where do you have the authority to float new bonds without going to the people?

MRS. FELKER: In the bond act.

SENATOR GALLAGHER: What bond act?

MRS. FELKER: Every individual bond act.

SENATOR GALLAGHER: The people approved the bond act that you could float new bonds?

MRS. FELKER: That's right.

SENATOR GALLAGHER: They did do that.

MRS. FELKER: If you look, it is found in Sections 20, 21 and 22 of most of the bond acts. It says "the issuing officials are hereby authorized to issue refunding bonds," and then it gives conditions under which they can do that.

SENATOR GALLAGHER: But, the people approve.

MRS. FELKER: The people have approved those, yes.

SENATOR GALLAGHER: That clears that up, thank you.

SENATOR WEISS: When was that approved, Liz, how long ago? Is it on every bond?

MRS. FELKER: Yes, it's standard language. It is worded almost identically in each one.

SENATOR WEISS: Did you hear that, Senator Rand

SENATOR RAND: I think I somehow understand it.

SENATOR EWING: Will you explain it to me, Walter?

SENATOR RAND: It took me a long time to get this myself, Jack.

SENATOR WEISS: You are not going to give it away cheaply, are you?

SENATOR EWING: Mr. Chairman, I have one more question.

SENATOR WEISS: All right, I'll save mine. Go ahead.

SENATOR EWING: You would not be floating bonds and holding the money until a later date to buy, you would float new bonds. You call those a part of the other bond issues, and would call them right then and there, right?

MRS. FELKER: No, that isn't what we would do. We would float the new bonds as soon as it made sense to do that under this new authorization. We would invest that money until the time came to call the bonds. In the

meantime, the investment earnings from the investments would pay the interest on the bonds that are going to be called. Then, at the end, the investment earnings would mature, and they would be maturing in an amount exactly equal to the principal amount of the bonds being called and the call premium that we would be required to pay. So, we would not disturb the bonds or the bondholders until the call date.

SENATOR EWING: Oh, that's right, because they were not callable until 1991. Okay, I'm sorry.

MRS. FELKER: What we have done is, we have taken advantage of today's interest rates for today's budget savings.

SENATOR EWING: But, aren't there certain bonds that have been issued, maybe, that have a callable date, but you did not have the money on hand so you did not call them?

MRS. FELKER: There have not been.

SENATOR EWING: All right.

MRS. FELKER: It was not the State's practice to put call provisions in its bonds until three years ago.

SENATOR EWING: Thank you.

SENATOR WEISS: Are there any other questions? Anyone else? Senator Gallagher?

SENATOR GALLAGHER: You do not consider increasing the State's debt when you are escrowing treasuries?

MRS. FELKER: Do you mean in the principal amount of the refunding bonds? Are we concerned about that?

SENATOR GALLAGHER: Yes, but I mean you do not consider that as increasing the State debt as long as you have treasuries in escrow.

MRS. FELKER: That's true, because you have an asset that you purchased with those funds which offsets that debt.

MR. FORRESTER: Senator Gallagher, if I also may add to that, I think we have to remember that there is no artificial limit on the State's indebtedness. The concerns about the level of State indebtedness that the Treasurer has may, from time to time, have to do with the assessment of how New Jersey is rated in the marketplace, and that is why we are concerned with this issue of whether or not borrowing more principal in order to fund or refund the existing debt would cost a concern, and the answer was a flat "no" from the rating agencies. It would not be a concern because, as was

mentioned, we would be purchasing an asset. Moreover, it would be a reduction in the amount of debt service that we would have to pay. I think it would be appropriate now to mention that Mr. DeSeve, who I referred to earlier, has participated in such a refinancing proposal for Alabama. This was a distinct advantage to Alabama, although their budget is structured differently than ours. The rating agency saw it as a plus that they were able to do that, because of the cash savings it gave them, even though their rating was in somewhat of a precarious position because of unemployment at the time. Their rating was not lowered, even though they were technically incurring more debt, because of the structure of the refinancing, which is really what we are proposing here.

SENATOR GALLAGHER: I don't want you to take any of these questions as being in opposition to the concept, because I think we all agree with the concept. We are trying to understand exactly which way you are going. Now, it would seem to me, although you indicated that Moody's and many standard employers have indicated they would not consider it as additional debt, that it is debt. You are just going to pay that additional debt with treasuries that you have in escrow.

MR. FORRESTER: I think that it would--

SENATOR GALLAGHER: But, there is still a State obligation to make the payments to those bondholders with the funds from the treasuries.

MRS. FELKER: Actually, we are paying the new debt with State funds, and the old debt with the treasuries.

SENATOR GALLAGHER: I understand that, but the State of New Jersey is still obligated to pay -- your source of revenues to pay is coming from the treasuries.

MRS. FELKER: That is correct.

SENATOR GALLAGHER: Thank you.

SENATOR WEISS: Senator Gallagher, I feel the same way about that as you do, that somewhere the State is a holder in due course, and still responsible, even though somewhere in all this paperwork it says that the State will no longer be responsible. I would consider that somewhere down the line, maybe in a couple of years, these nice folks in the rating agencies are going to come back and say, "Well, you know, you are really responsible for it." But, maybe it is worthwhile taking a chance if we can save \$20 million a year. That is not money to be sneezed at.

Liz, could you tell me how much is available in this refinancing for refunding bonds now? How much can we do next year, or this year as a matter of fact, since we are just starting it?

MRS. FELKER: If this passes in November, and then if the Legislature passes a bond act--

SENATOR WEISS: Let's assume it all passes.

MRS. FELKER: Okay. We could refinance both of those two high coupon issues. The savings that we would realize would be a function of the interest rates at the time. Those are the bonds that we issued; there are a number of series within these.

SENATOR WEISS: Do you have a rough dollar amount?

MRS. FELKER: There are \$285 million of principal amount outstanding.

SENATOR GALLAGHER: If you could do it today, how much would you save, and at what rate?

MRS. FELKER: Okay. A portion of that, \$135 million, is at 12.1%; \$150 million is at 11.6%. We have made one principal payment.

SENATOR WEISS: We are now down around nine, is that right?

MRS. FELKER: Our last issue was-- We were very fortunate in hitting the lowest rate we could have had so far this year in April. We issued term bonds at 8.2%, and serial bonds at 7.5%, with an average overall cost of 7.8%. That was a very fortunate result for New Jersey. So, that is a big difference. Today, we are somewhere closer to 9%. The amount of savings that could be generated in dollars-- Our function of the interest rates at the time the refunding was done, we decided to try a couple of different interest rates to see how much they were, and then how sensitive they were to interest rates. I did this with the assistance of Mr. Fowler, who is behind me. If we were to refinance all those bonds at a rate of 8.6%, we could save \$5 million -- I'm rounding these off -- on the 11.6% bonds, and \$5.7 million on the 12.1% bonds. Now, that is at 8.6%.

SENATOR GALLAGHER: That is over the life of the issue?

MRS. FELKER: That is the present value of the savings.

SENATOR GALLAGHER: Over the life of the issue?

MRS. FELKER: Well, let me tell you what happens if interest rates go lower, and then I'll tell you when you can have the money. If interest rates were to go down to 7.2%, which is 140 basis points lower, those savings

would increase dramatically. The savings on the 11.6% bonds would go up to \$9.4 million. The savings on the others would reach \$9.9 million. So, you are looking at almost \$20 million. Now, when are those savings available? Those savings are available either over the life of the issues, spread out over twenty years, or they can be available during a shorter period of time. A deal could be structured to provide it to you all in one year if you so desired.

SENATOR WEISS: It suddenly occurs to me, Liz-- I got this thought, and I don't know if it is a good one or a bad one at this point. But, it suddenly occurs to me that you are talking about rolling over that which has already been rolled over, and which will be rolled over for a second, and a third, and maybe a fourth time. Is that what you are saying?

MRS. FELKER: I have not proposed that.

SENATOR WEISS: Well, I just got the impression that this year since we are at 12.1, you are going to roll those over at 8.2% with the refinancing thing and, if interest rates go lower -- you said, "Tell me when interest rates go lower, and I will tell you what I am going to do at the time," or at least that is the way I remember it -- then, are you considering a second and a third rollover in the same series of bonds?

MRS. FELKER: First, let's say that we keep the final maturity constant, so we do not extend the life of our debt any further. But, there are refunding--

SENATOR WEISS: We do not like to have that over with right away.

MRS. FELKER: You could put refunding provisions in the refunding bonds. That is up to the Legislature. If it does not want to have them refundable, it can say, "No, we do not want to put refunding provisions in those bonds." You could make those callable or noncallable.

SENATOR WEISS: Senator Gallagher?

SENATOR GALLAGHER: Yes, I have just one question. You are talking about refinancing \$285 million of the \$300 million. Half of it -- well, not quite half of it -- is the protected area not subject to call.

MRS. FELKER: We could do that, or not do that. We are really talking about only the \$170 million that is callable.

SENATOR GALLAGHER: But, you gave us figures on \$285 million. Now, what kind of figures do you have on that which is subject to call?

MRS. FELKER: It would be the same.

SENATOR GALLAGHER: The same? Why then would you roll over \$285 million?

MRS. FELKER: There is no reason to refund the noncallable bonds unless we decide to change the maturity structure within that period.

SENATOR GALLAGHER: Okay, so then out of the \$300 million, you are talking somewhere around \$150 million.

MRS. FELKER: Well, \$170 million is about what it comes out to in terms of the amount we would need to pay off the principal and the premiums.

SENATOR WEISS: Senator Ewing? Thank you, Senator Gallagher.

SENATOR EWING: What would be the administrative costs of doing this, you know, for bonding attorneys and people like that -- the lawyers who make all the dough?

MRS. FELKER: They would be approximately the same as to do our normal bond issues.

SENATOR EWING: What would it be on a \$170 million issue then, period?

MRS. FELKER: It would probably be around \$200,000. However, that would--

SENATOR EWING: (interrupting) The total cost of printing, and lawyer fees?

MRS. FELKER: Yes, that is about what we are paying.

SENATOR EWING: Thank you, but I still don't like the statement.

SENATOR WEISS: All right, the statement does appear somewhat ambiguous, but I think it puts forth what they are trying to tell us.

SENATOR EWING: Who made up the statement?

SENATOR WEISS: The Treasury, who else? Why do you think it is ambiguous.

MR. FORRESTER: Mr. Chairman?

SENATOR WEISS: Mr. Forrester.

MR. FORRESTER: May I make a follow-up comment with regard to this issue? I think one of the things that needs to be emphasized has to do with the participation of the Legislature in these refinancing proposals. We spoke earlier of the fact that currently after the call date the Administration can, without the participation of the Legislature, proceed to refund something. This is a refunding proposal which would require the approval of the Legislature for any kind of refinancing proposal. I think

that that is important. There would have to be an agreement between the Executive and the Legislative Branches on the wisdom of refinancing. I think that that kind of cooperation is a good thing in this regard. I think it would allow an opportunity for any information from the rating agencies, which someone might suggest could be adverse, to be evaluated. I think there would be time enough to have a flexible refinancing proposal go through in an expeditious way, and yet allow for the kind of scrutiny that everyone would desire. Lest there be any uncertainty with regard to this issue, the State being obligated still to pay off the existing debt, I think it is very, very important that we all appreciate the fact that these are U.S. government securities that are being purchased. That kind of grounding for the payment of the existing State debt is extremely important. The reason why is because if we cannot trust U.S. securities, then there is no reason to make any kind of bets. All bets are off, so to speak.

SENATOR WEISS: Doug, I couldn't help but recognize the great stress and generosity about giving this power to the Legislature, and you keep stressing it all the time. And, I am wondering why you are being so kind to us.

MR. FORRESTER: Well--

SENATOR WEISS: Give me the caveat. I can't stand so much in this line.

MR. FORRESTER: I think my origins are coming out here.

SENATOR WEISS: Does this go back to the Mosaic law somewhere?

MR. FORRESTER: In terms of my sympathies for legislative oversight in these matters. There isn't any sort of quid pro quo or anything like that. We are dealing with the fact that we think this is important. We realize that we are amending the Constitution in an area that has to do with public oversight and levels of indebtedness, and we want to make sure that everyone in the public is confident that these refinancing proposals will receive the full airing of public debate. The best way to ensure a full airing and scrutiny of these issues by the public, is to invite legislative oversight and participation in the approval of these refinancing proposals. So, because of the nature of the constitutional section that we are amending, we think it would be most prudent, and that everyone would feel most comfortable, if the Legislature were to have the final say on approving these refinancing proposals .

SENATOR WEISS: I accept your explanation. It seems rather unusual, however.

SENATOR EWING: I don't think the public will like it though.

SENATOR WEISS: Senator Gallagher has another question.

SENATOR GALLAGHER: I have one other question. It has to do with reluctance to changing the Constitution, which is there, and has been there for years, for the protection of the public. If we are talking about that portion of the issue that is subject to call, you have the right, right now, as you say, by the voters of the public when they approve that particular bond issue, to do what you want to do. Why do we have to change the Constitution?

MRS. FELKER: We do not have to change the Constitution if you are willing to wait until 1990 to get the benefit of lower interest rates. If you would like to take advantage of those lower interest rates now, we have to change the Constitution.

SENATOR GALLAGHER: Okay. What you are saying is that when you went to the voters for those particular bond issues, you put into what they voted on that you could not refund anything after the call until the call date. Is that right? And, if you went to the voters next year with a new bond issue and put in there that you could have the right to refinance that issue for the bonds that were subject to call prior to the call date, you get the same thing, don't you?

MRS. FELKER: You would, but do you know what you would have to do? You would have to change the way you describe that public question to include the refunding bonds in the public question, and you would even have to express the dollar amount of refunding bonds that could possibly be issued in that public question. So, you would be faced with saying, "\$200 million worth of bonds for public buildings, and \$240 million to refund those bonds." I think, and most of the rest of us think, that that is an awful big thing for the voters to swallow, and that they are all going to think we are all bananas here, putting something like that on the ballot. It seems a little more rational to deal with it in this fashion, and to say that we would like permission to refund in order to save money, without going into detail in the ballot question on two different dollar amounts of debt which seem to be additive.

MR. FORRESTER: I think, Senator, that it would also be worthwhile to point out that it isn't helpful for us to speculate on what the economic conditions are going to be like ten years from now, and the financial decisions that are going to be made at that time have to be made at that point in time, not now.

SENATOR GALLAGHER: Yes, I understand that, but I'm saying that if you went to the voters and you had in there the right to refund on a particular issue, as against a blanket change in the Constitution, that would give you the same thing that you want on future bond issues. It wouldn't cover these two.

MRS. FELKER: It would not cover outstanding bonds. We would not be able to do anything about those two.

SENATOR GALLAGHER: No, it wouldn't cover these two.

MRS. FELKER: We have considered that, and what we end up with is this very complex public question. It seems unpalatable to ask the voters to approve that. It seems too complex.

SENATOR GALLAGHER: I would not give you permission if you used the figures you used.

MRS. FELKER: That's right, and that is exactly the way it would read.

SENATOR GALLAGHER: Two hundred and forty million dollars.

MRS. FELKER: When we saw the way that would read, we said, "No, this will not work. We will not be able to accomplish it this way."

SENATOR GALLAGHER: What concerns me is that the thing that you are talking about that you do not want to go to the voters for, is what you are asking us to give you the right to do.

MRS. FELKER: That is what Senator Weiss was asking, "Why are you asking the Legislature?" We have to believe you are better able to comprehend that than the rest of the public.

MR. FORRESTER: Senator, I can appreciate--

SENATOR EWING: Is that what you said, Doug, that we were stupid?

MRS. FELKER: He said you were smarter.

SENATOR EWING: Oh, okay.

MR. FORRESTER: Senator, I think the answer to your question is an important one, and the response I gave to the Chairman when he asked why we feel it is important to have legislative participation, is that we want the

public to have confidence that these things are being evaluated by capable people in the ways they should be. We are confident that the best policy to form for this to be evaluated is in the Legislature. It provides opportunities like this to come to lay out a computer sheet and be able to walk through the calculations that are made, to be able to demonstrate the kind of savings, and to answer questions. I think you can all appreciate the fact that this is really not possible to do on a public question and really treat the voters fairly.

MRS. FELKER: I would like to expand on the answer I gave Senator Ewing about issuance expenses, if I may.

SENATOR WEISS: All right, Liz.

MRS. FELKER: Senator Ewing, you had asked about how much the issuance expenses were, but I did not tell you how we would pay for them. I could have told you, and I will now, that the rules of the U.S. Treasury would allow us to invest our proceeds of the refunding issue at a rate sufficient to cover, not only the principal and interest payments we would be making with that fund, but also those issuing expenses. So, this would not be a cost that we would pay out of pocket. This would be covered in the investment earnings. The arbitrage regulations are now broad enough to allow this. This has been recently established.

SENATOR WEISS: If the rate is low enough?

MRS. FELKER: Surely. You wouldn't be able to do it unless the rate was low enough. The reinvestment rate has to be--

SENATOR WEISS: (interrupting) I just wanted to make it clear to the Committee that there is a problem with a low rate.

MRS. FELKER: There is a balancing that is done when these types of financings are executed which trades the principal amount of the new bonds, the interest rate on the new bonds and the reinvestment rate which is available on those U.S. Treasury securities. You plug all of those into a formula. It can be done by computer, but it can also be done by people. There are people who understand it well enough to do it themselves to figure out what the right dollar amount to issue is, and what reinvestment rate is required.

SENATOR EWING: Well, when you buy the bond from the Federal government, do they give you a special issue for New Jersey?

MRS. FELKER: That's right. What we are really doing is, we are financing down for a period of time with our money, you see? We are lending them money over a period of time so they earn interest on it. But, they tailor those issues for our benefit, that's right. They are called SLGS, State and Local Government Series.

SENATOR WEISS: Liz, just to give everyone in the audience, and the Committee, a practical application of what is going on, let's assume that the original issue of the bond was \$100 million. You have now paid down to \$50 million, and there is still \$50 million to go. Who, in fact, decides that now is the time -- and don't tell me the Legislature, okay, unless that is going to be fact -- to refinance these bonds, and is it done on the basis of a balance, or is it done on the basis of a percentage?

MRS. FELKER: It would be the Treasurer's responsibility to make that recommendation.

SENATOR WEISS: And he makes that recommendation to whom?

MRS. FELKER: Well, first he would make it to the Controller and the Governor, who constitute the issuing positions.

SENATOR WEISS: Then it will come in the form of a bill to the Legislature?

MRS. FELKER: It will come in the form of a bill to the Legislature. The amount that would be issued would be determined by analyzing the interest rate in the market at the time, then deriving from that a maximum principal amount that would have to be authorized in order to enable enough funds to be issued to get savings at that rate.

SENATOR WEISS: So, then there is a ratio between the amount paid off, the amount left in the balance, the rate of the original issue, and the rate of the new issue?

MRS. FELKER: That's right. It is not a direct ratio. The amount of bonds to be issued goes higher as the interest rates go lower.

SENATOR WEISS: That is the thing I want you to explain, that determination between the balance of the \$50 million and the balance that you have to pay off, and how the amount is raised in ratio, as a matter of fact, with the interest rate of the new amount.

MRS. FELKER: In order to generate enough interest to pay off the old bonds if interest rates are very low, you are going to need to invest more dollars to get the right flow of cash to come out. If interest rates

are higher, the investment rate is going to be higher and we would need to borrow less to generate the same amount of cash flow. So, you look at what cash flow you need, what the interest rates are, and how much you would have to invest at those rates to get that cash flow. That is what you do.

SENATOR WEISS: Okay, thank you. Does the Committee understand that? (affirmative response)

MR. FORRESTER: Mr. Chairman?

SENATOR WEISS: Mr. Forrester.

MR. FORRESTER: May I just mention further that it is difficult to come up with an exact figure at which point this refineness in the proposal would be possible. However, I think it would be workable to say that somewhere between 2% and 3% you pass that threshold. I would have to calculate all the costs incurred and the interest rate differentials, to determine that it is a viable proposition.

SENATOR WEISS: I think, Mr. Forrester, that that is understood. I just wanted a clarification of it for those who are here, so that no one goes away confused about what is really going to happen. I mean, anymore confused than they are now. Are there any further questions? (affirmative response) Senator Gallagher?

SENATOR GALLAGHER: You indicated before, Mr. Chairman, that they could refinance for reasons other than just improving the debt service. Where did you see that, because if there are other reasons, I would like to get a list from Treasury of what is in our bond issues now that they might consider as falling in those categories? You were talking about the source of funds and everything else.

SENATOR WEISS: I read it somewhere here, Jack.

SENATOR GALLAGHER: Yes, but I mean Mrs. Felker was talking about the source of funds, etc., to pay for the bond issue.

MRS. FELKER: Should I respond to that?

SENATOR GALLAGHER: Yes, I would like to know some of the areas that you are talking about.

MRS. FELKER: I have no areas at all that I would recommend doing that for. I only observe that it is a possibility in a refunding to do different things other than save money. The only motivation that we have at this point is to do that and I, quite honestly, know of nothing I would change, nor would it be really feasible to try to do that, given the fact

that there are so many uncallable bonds outstanding. It would be pointless. Any changes that we have to make in bond issues, we are making in new bond issues to conform with new requirements of the registered bond arena, and to build in flexibility to sell bonds as term bonds instead of serial bonds. But, we have not done that retroactively. It would be nice to do that, but it would be impossible to accomplish.

MR. FORRESTER: Senator Gallagher, I also want to underscore the fact that the specific language of the constitutional amendment specifies that it is only in cases in which debt service savings can be realized. So, if debt service savings are not realized, regardless of what other reasons may be deemed worthwhile, we would not be able to come up with a refinancing proposal.

Now, if indeed debt service savings are realized, and there are other sorts of considerations that are, let's say, noticed in terms of a refinancing, they can be evaluated on their variance, and the Legislature, obviously, would be doing that.

SENATOR GALLAGHER: Okay. Now, you raised a point -- while the Chairman is looking through his notes-- How much are the all registered bonds going to cost us in the State?

MRS. FELKER: In terms of--

SENATOR GALLAGHER: In terms of handling them, transferring them, and everything.

MRS. FELKER: For the State itself, I don't suspect it will be a very large charge. We have not yet put out a proposal to banks to serve as registrar. We are about to do that. Then we will be better able to answer that question. I don't think it is going to be a great deal of money that will cause huge concerns. It will be somewhat more than what we are paying paying agents.

SENATOR GALLAGHER: Would you let us know?

MRS. FELKER: Surely.

SENATOR GALLAGHER: Thank you.

SENATOR WEISS: I can't seem to find that at the moment, Senator, but it was in one of these papers.

MRS. FELKER: As to the reasons?

SENATOR WEISS: Yes, the other reasons other than the interest.

MRS. FELKER: That was in this (witness holds up paper Chairman was looking for).

SENATOR WEISS: Oh, I knew I read it somewhere.

MRS. FELKER: I'm reading from a research report from an analyst at Merrill Lynch. The reasons for refunding-- One reason is to remove restrictive bond covenants; another is to change the debt maturity schedule; and, the third is to save money, which is our motivation here.

SENATOR GALLAGHER: What you are talking about here is strictly saving money.

MRS. FELKER: That is what we are talking about, yes.

SENATOR WEISS: And, the other two will not enter into it.

MRS. FELKER: No, they need not.

SENATOR WEISS: Just answer the question. We are not sure. They need not?

MRS. FELKER: No. The reason I can't say that is because I cannot tell what you will pass in the way of a refunding bond act.

SENATOR WEISS: I think all of us on the Committee approve the situation, but there seems to be some question about some of the things, and that would be one, at least it would be mine. I think Senator Foran was a little concerned about something like that before.

MRS. FELKER: I won't be able to give you a specific assurance there, because there is another piece of legislation required and it will have provisions. I know what we would propose, but I cannot predict the outcome.

SENATOR WEISS: That's true.

SENATOR GALLAGHER: One last question, do you have anything in writing from Moody's or standard employers relative to that matter of additional debt?

MRS. FELKER: No, I don't.

SENATOR GALLAGHER: You do not.

MRS. FELKER: We did not ask them for a written statement.

SENATOR GALLAGHER: But, they have indicated to you that they would not consider this additional debt?

MRS. FELKER: That's right, they have. But, I think it might be more useful to look at their past decisions on other issuers who have done refunding bonds and whether, in fact, they have penalized anyone for doing

this type of thing. If you would care to get into that in more detail, we can do that. We know of no case where people have been penalized for issuing refunding bonds to achieve savings even though they had to incur additional principal on the amount of debt.

SENATOR WEISS: Are there any further questions? Senators Ewing, Gallagher, Foran or Rand? (negative response) Then, I think maybe we should hear from Mr. DeSeve of Merrill Lynch. Mr. DeSeve, do you have anything you can add?

MR. DESEVE: No, sir.

SENATOR WEISS: That is a graceful way out. How about Mr. Fowler?

SENATOR EWING: Ask him if he would vote for it if it was on the ballot the other way.

SENATOR WEISS: Would you vote for it if it was on the ballot and you were not with Rothschild and Merrill Lynch? (affirmative response) You would?

SENATOR RAND: How about Frank Haines? I would like to hear what he has to say.

SENATOR WEISS: I talked to Mr. Haines before and he said he had nothing to say. Mr. Haines, would you like to express an opinion on this?

MR. HAINES: No, Senator. (comments further from audience, but cannot be heard)

SENATOR WEISS: I turned it down for you.

MR. HAINES: Thank you very much.

SENATOR WEISS: Doug and Liz, I guess that will be all for this morning, unless there is someone else who would like to say some famous last words. If not, we thank you for your appearance here this morning, and thank you for the lesson in finance. There is no release on this; this is a public hearing, so we will just adjourn the meeting.

MR. FORRESTER: Mr. Chairman, let me first thank you for your sponsorship of the proposal. I very much appreciate your consideration of our comments today. Let me say that we are eager to answer any and all questions at anytime, and we would be happy to provide any material that the Committee may think appropriate.

SENATOR WEISS: Doug, it would appear to me that before this thing goes all the way through the process, that we will have Liz back, and you, and possibly Treasury Biederman, if he is in town. We will look forward to seeing you then. Thank you.

(HEARING CONCLUDED)

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