

December 21, 1999

The Honorable Tony Knowles
Governor
P.O. Box 110001
Juneau, Alaska 99811-0001

Re: Financing Methods for State
Capital Improvement Programs
(Transportation-Related Projects)
A.G. file no: 663-00-0064

Dear Governor Knowles:

You have requested our analysis of certain techniques to finance capital improvement projects from discrete sources of revenue. These sources include future reimbursements of federal highway grants and tobacco settlement proceeds.

FEDERAL HIGHWAY FUNDS

Federal law now allows the states to use federal highway funds to cover debt service for bonds issued to cover projects qualified for federal financial participation. Sec. 311, National Highway System Designation Act of 1995. This has enabled some states to issue grant anticipation instruments known as GARVEE bonds. GARVEE bonds are long-term debt instruments which are repayable either exclusively or primarily from federal highway funds to be received in the future. It is not possible in Alaska to pledge federal funds to secure these bonds because the state constitution limits the ability to anticipate revenues, including federal highway grant reimbursement revenues. There may also be impediments under the dedicated fund prohibition.

Consequently, it would be possible to finance certain transportation-related projects using the process to issue general obligation bonds. These *federal revenue general obligation bonds* would be secured by the state's general promise to repay the debt from any generally available revenue source, or to undertake any other means to raise sufficient revenue to retire the debt. However, depending on the structure of the transaction, the voters could be advised that it is the intent that debt service would either entirely or substantially be covered out of appropriations of federal highway grant reimbursements. These bonds must be authorized in a bill enacted by the legislature and ratified by a majority of the voters casting ballots on the question. Alaska Const. art. IX, sec. 8.

There are some legal issues bearing on your budgeting powers regarding projects set out in a bond authorization bill. The legislature has passed a statute requiring that bond authorization bills specifically identify the scope of each project, location, and amount allocated. AS 24.08.037. The Director of Elections is required to provide a statement of the scope of projects along with the sample ballot provided to voters. AS 15.15.040. Even though the authorization bills are worded much like an appropriation of the bond proceeds for the projects, the Alaska Supreme Court has held that they are not appropriations and that your line item veto power does not apply to these bills. *Thomas v. Rosen*, 569 P.2d 793 (Alaska 1977). On the other hand, bond authorization bills are usually prepared in way that allows the reallocation of authorization between projects by the department charged with construction of the capital improvement being financed.

We believe that you should take the position that projects will not be undertaken unless appropriations of bond proceeds are made in the state's capital budget. By doing this you can use the line item veto to prevent the log-rolling of improvident or ill-advised projects along with those that have some prospect of meeting the public interest.

LEASE PURCHASE

Another means of financing capital improvements is through lease-purchase financing. This method does not involve the creation of debt and therefore does not require a ratification vote to authorize the transaction. However, the legislature must authorize the financing after being advised of the costs associated with the lease. AS 36.30.085(d) and (e). Under this method, capital improvements that consist of a public facility are financed by selling rights to receive a part of the payments made by the state under a lease agreement for the facility. The lease transaction is an internal arrangement where lessor and lessee are both public entities. The rent obligation under the lease would be conditioned on the enactment of sufficient appropriations of federal highway grant reimbursements or of other sources determined by the legislature.

Generally, the facility to be financed must be for an essential public purpose and constitute appropriate security for the transaction. That is, there must be an ability to deprive the state of its use in the case of default on the payment of rent. This financing method works well for assets like vessels, mainframe computers, public buildings, and other discrete facilities. It would not work well for major highways and other improvements for which there is little or no possibility of effectively enforcing a deprivation of use in case of default.

TOBACCO SETTLEMENT PAYMENTS

Another possible financing method involves using the stream of payments generated by the settlement with manufacturers of tobacco products. The anticipation of this revenue stream is subject to the same constitutional limitations discussed above in connection with GARVEE bonds. It might be possible to sell the right to receive this stream of revenue and recover the present value of this money to finance capital improvements. The purchaser of this

The Honorable Tony Knowles, Governor
A.G. file no: 663-00-0064

December 21, 1999
Page 3

right would be a public corporation that raises the purchase price by selling revenue bonds secured by the rights obtained from the state.

I hope that this brief explanation of financing techniques will serve your purposes.

Sincerely,

BRUCE M. BOTELHO
ATTORNEY GENERAL

By:

James L. Baldwin
Assistant Attorney General

JLB:jn