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MTF Session Preview: Capital Spending

Each year, Massachusetts spends billions of dollars on capital infrastructure and investment, but the process that guides that spending is not well understood in comparison to the annual budget process. This session, the Healey administration and the legislature will take up several major bond bills that will shape future capital spending. Policymakers will also struggle with very real constraints on borrowing that will force difficult decisions on what capital investments are possible.

This preview outlines how infrastructure spending works and highlights important capital planning decisions to be confronted over the next two years.

Background

Capital spending means investments to maintain or build capital assets – infrastructure like roads, buildings, software systems that will benefit the Commonwealth and its residents for years to come. Because the benefits of capital projects extend into the future, the state primarily pays for them by selling bonds which are repaid through debt service payments over the useful life of the project.

Legislation that governs the sale of bonds and determines how proceeds will be used are referred to as 'bond bills.' These bills typically authorize the sale of bonds to support five years of a capital plan in a specific policy area. This means that at least every five years, or so, there is a new environmental bond bill, public safety bond bill, or a transportation bond bill.

Each bond bill authorizes a maximum amount of bonds to be sold, the length of time to repay the bonds, sets forth capital spending areas on which the bond proceeds can be spent – referred to as bond authorizations, and sometimes identifies the federal share of major programs. Under the Constitution, the legislature must approve most borrowing by a two-thirds majority. This means that bond bills must occur in sessions when roll calls can be recorded.

The administration has significant discretion to determine if, when, and how much in capital resources will be used for a specific authorization. This process differs from the operating budget: in the annual operating budget, barring midyear budget cuts or other unique circumstances, the administration is required to pay out spending items that are signed into law. In the capital budget, there is no requirement that the administration devote any resources for a specific item. As the name implies, a capital authorization allows the administration to use resources in a certain way, but does not require it.

The reason for the broad discretion granted to the Executive Branch, is due to the fact that actual capital spending, supported by debt, is limited by both statute and policy and the amount of spending authorized often exceeds those limits. Therefore, the administration must prioritize various capital spending needs to fit within those constraints. Those priorities are announced in the annual five-year capital plan, released by the administration in late spring or early June.

In FY 2023, the five-year capital plan calls for $2.78 billion in capital investments supported by general obligation bonds. This category of capital spending falls within the 'state bond cap' – an administrative limit on the amount of capital spending supported by bonds backed by the state's General Fund and not by a specific revenue source. Those investments are organized into the following policy areas:

Category	Amount
Transportation	$1,108
State buildings	$608
Environment, energy & climate	$270
Housing	$261
Economic development	$245
Information technology	$175
Public safety	$30
Education	$22
Other	$61
Total	**$2,780**
$ in millions	

Understanding the capital spending plan is made challenging by the fact that the state bond cap described above, does not apply to a variety of infrastructure resources, such as federal funding, capital spending supported by special obligations (borrowing with dedicated revenue sources), and several smaller types of investments. It also does not include capital investments by agencies like the MBTA, MSBA or MWRA, which borrow against their own revenue sources. The fact that bond bills only provide authorizations for spending and significant investments that occur outside of the state bond cap make the capital spending process much more opaque and difficult to track than the operating budget process. The annual five-year spending plan is the primary document available to understand capital decisions, but unfortunately the amount of information included in that document has become increasingly limited.

Capital spending in Massachusetts is constrained by several policies. By law, the state has a statutory debt limit, which limits the amount of the Commonwealth's outstanding direct bonds. In FY 2022, that limit was $27.8 billion and the amount of outstanding direct debt was $23.9 billion. In addition, the state has a debt affordability policy which limits annual debt service payments (spending necessary to repay bonds) to less than 8 percent of budgeted revenues. In FY 2022, this limit was $4.3 billion. Further, the Patrick and Baker Administrations followed a policy that capped annual capital budget growth at $125 million per year. In light of these limitations and the fact that Massachusetts has among the highest debt per capita in the nation, the administration's capital spending plan is informed by a Capital Debt Affordability Committee which recommends a prudent level of capital spending each year.

Transportation and upkeep of state buildings have historically been the largest categories in capital spending, but recent capital investments for information technology, climate change adaptation, and housing have increased significantly, putting greater strain on available resources.

Key Policy Actions, 2021-22

Soldiers' Home Investments – In May of 2021, Governor Baker signed a $600 million authorization to rebuild the Holyoke Soldiers' Home and make other investments in long-term care services for veterans. The administration's FY 2023 capital plan estimates that $40.5 million will be spent on the new Holyoke facility over the next three years, with a further $35.4 million planned for other soldiers' homes investments.

Municipal Road Funding – The state's Chapter 90 program, which provides state aid for municipal road maintenance and projects, is funded through the capital budget. In both 2021 and 2022, the state provided $200 million in Chapter 90 aid through the capital budget. In FY 2022, the state provided an additional $100 million in operating funds for winter road repairs in cities and towns. On January 19th, Governor Healey filed the first bond bills of her administration, including a reauthorization of the Chapter 90 program. She included a 2-year, $400 million authorization; the bill has been assigned to the Joint Committee on Transportation.

General Government Bond Bill – In August, Governor Baker signed into law a $5.2 billion general government bond bill which authorized five years of capital investments for state assets. The largest authorization ($975 million) is for planning, purchasing, repair, and leasing costs for state buildings overseen by the Department of Capital Asset Management and Maintenance (DCAMM), but other large authorizations were provided for projects specific to certain policy areas:

- Health and human service facilities – $820 million
- Public higher education institutions – $750 million
- Trial court facilities – $675 million
- Public safety facilities – $530 million, with $50 million earmarked for immediate capital improvements to Bridgewater State Hospital
- Decarbonization and climate mitigation at state buildings – $400 million
- Food security grants - $51 million

In addition, the bill includes more than 300 local capital earmarks, which add up to more than $200 million. The inclusion of these earmarks, however, does not mean that many or even most will ever be included in the state's capital budget. Lawmakers and supporters of earmarked programs will need to work with the administration to make the case for future capital funding.

Transportation and Climate Resources – The legislature acted on an $11.4 billion authorization bill designed to maximize federal capital funds for transportation and climate projects. Included within the $11.4 billion total is just under $4 billion in expected federal capital funds, for which the state needs to provide a match. The largest investments in the bill are:

- Discretionary transportation grants funded thorough the Infrastructure Investment & Jobs Act - $3.5 billion (federal share of $1.75 billion)
- Federal road projects – $2.8 billion (federal share of $2.2 billion)
- MBTA and commuter rail improvements - $1.375 billion
- State and municipal roads – $1.3 billion (no federal share)
- Electric vehicle charging infrastructure - $225 million (no federal share)

This bill also authorized more than $1 billion in authorized funding for close to 500 local project earmarks.

Economic Development Authorization Falls Short – Every two years, the legislature passes an economic development that includes policy proposals and authorization for investment in economic development and housing capital programs. The House and Senate versions of this year's economic development bill included about $1.5 billion in capital authorizations, but they were not included in the final version of the bill. The reason for the omission was that by the time the bill was negotiated, formal sessions for the year had ended. Because capital authorizations require roll call votes, the House and Senate could not authorize the borrowing and therefore have to wait until this session to act.

Policy Context

The state's infrastructure needs are significant and expanding into new areas at a time when our capacity to borrow is limited. While significant additional federal resources are available in the near-term, the tension between goals and capacity will be at the root of capital spending decisions made this session.

Significant & Growing Needs

For years, transportation and the physical condition of state-owned buildings have driven the state's capital budget, and those needs have not gone away. In fact, pressures on the transportation capital budget have increased as years of underinvestment and new projects have required resources. MTF estimates that the capital backlog at the MBTA, for example, is at least $12 billion for necessary upgrades and repairs to the current system. At the same time, new capital priorities have emerged. In the last ten years, the amount of the state bond cap devoted to information technology has doubled, while the amount dedicated to housing has grown by more than 60 percent. Ten years ago, climate change mitigation and preparedness were not even part of the annual plan and now are an area of focus. Capital funding for environmental, climate and related projects is more than double its FY 2013 level and that investment is likely to grow significantly with the next environmental bond bill. However, current capital investments related to climate policy only scratch the surface of future needs.

In order to meet the state's clean energy goals, the state's energy grid will need to be completely overhauled. The state's 2050 Decarbonization Roadmap estimates that, in order to meet net zero emission goals, the state's grid will need to more than double its capacity and adapt to new generation sources. While much of these capacity changes will occur on privately owned infrastructure, grid changes have huge implications for the state's transportation and public building capital needs.

Climate and environmental adaption will also require capital investments not accounted for in state or local capital plans. In 2021, the American Society of Civil Engineers estimated that the state's drinking and wastewater systems require $20 billion in capital improvements and this figure does not include the cost of improved storm-water management. The Massachusetts Clean Water Trust, separate from the state's annual capital plan, provides low-interest loans for local water infrastructure projects, but the annual outlay of the trust is not sufficient to meet the backlog of need.

Constraints on Spending

While demands on the capital budget grow at a rapid rate, constraints on capital spending remain. Massachusetts is one of the highest debt states in the nation, ranking behind only Connecticut in state debt per capita in 2020, and third in debt as a share of state GDP.[1] Part of the reason for this is because in Massachusetts the state assumes responsibility for many projects that would be under the purview of county or municipal government in other states. Nevertheless, the amount of state debt constrains future growth.

The state created a debt affordability policy in 2009 to put in place limits on future capital spending and ensure the state had a sustainable financial plan. The policy caps the growth of regular capital program to $125 million each year, or about 4 percent growth in FY 2024, and limits debt service to eight percent of budgeted revenues. Even with this limited rate of capital spending, modeling from the state's Capital Debt Affordability Committee shows that the state could run up against debt service spending caps within the next 20 years.

Temporary Federal Opportunities

Additional federal resources provide one opportunity to meet growing capital needs in spite of limited resources. The American Rescue Plan (ARPA), the Bipartisan Infrastructure Law (BIL), and the Inflation Reduction Act (IRA) each include significant new funds for existing capital programs and new initiatives which provide either guaranteed funding for states or competitive grants. The dedicated federal funds will be used to supplement the state's capital plan and in FY 2023, federal funds will add more than $1 billion to the state's $2.78 billion capital plan. Competitive capital grants are much harder to predict, but have the potential to accelerate progress on the current plan and enable the state to take on new projects that otherwise might not be possible. Discretionary federal funds have been essential to the biggest infrastructure projects the state has embarked upon in recent decades, including the Big Dig and the Green Line extension. With recent federal legislation, a similar opportunity exists for climate and other infrastructure priorities.

[1] Part of the reason for Massachusetts' comparatively high debt is that in many statues counties and communities take on a larger role in public capital spending.

Key Questions for the Upcoming Session

What is the plan to meet significant infrastructure needs not accounted for in the current capital plan?

Maintaining our transportation system, transitioning to clean energy, and preparing communities for the effects of climate change each require infrastructure investments not fully accommodated in current capital plans. In order to meet our infrastructure needs, the first step is to clearly lay out where we want to go. The annual capital plan does a good job of identifying specific projects to be funded over a five-year period, but does not lay out how those investments fit into a coordinated, long-term infrastructure plan. The Healey Administration should establish integrated, long-term, trackable, infrastructure goals for priority areas. That plan can assess how the various capital resources, state capital plan, federal funds, quasi-governmental agencies, fit into a long-term investment strategy and where the gaps are.

How can Massachusetts position itself to win competitive federal infrastructure dollars?

It is imperative that Massachusetts take full advantage of the opportunity for additional federal capital funds. Ambitious infrastructure projects in transportation and climate will simply not be possible without major support from Washington. To win that support, Massachusetts has to demonstrate that we are prepared to meet federal match requirements and quickly begin projects. In the capital budget, this means building on the Baker Administration's proposal to set aside flexible capital funds to serve as the state match for competitive grants when they occur. The legislature should authorize several hundred million in capital funds that the new administration can use flexibly in support of state applications for federal dollars. In exchange, the administration should work with the legislature to agree on the list of priority projects seeking federal support.

How quickly can the legislature act on housing and economic development capital programs?

The clock is ticking on reauthorizing capital spending for a number of critical infrastructure programs for economic development and housing. Because the final economic development bill was not passed until formal session had ended for the year, the House and Senate were forced to strip out $1.5 billion in capital authorizations. In January, Governor Healey filed a bond bill which includes more than $950 million of the authorizations that were not approved last session. More than $600 million of this total reauthorizes existing programs; without prompt action, programs like MassWorks will lack the spending authority to continue the program.

What will be included in the next environmental bond bill?

The state's last environmental bond bill (EBB) was enacted in 2018 and authorized $2.4 billion in state borrowing for five years of capital spending for a variety of climate, transportation and environmental infrastructure programs. Those authorizations will soon expire and it is very likely that a new environmental bond bill will advance this session.

Emissions reduction incentives, funding for parks and open space, as well as climate change mitigation will all rank high on the priority list, but water infrastructure should be front and center in policymakers' plans. Communities around the state face several water infrastructure challenges.

In many communities, old pipes degrade water quality and run increasing risk of breaking down totally. In other areas of the state, forever chemicals like PFAS render water unsafe to drink and their systems now require costly remediation efforts. Finally, our storm-water runoff systems are not sufficient especially as severe weather events become more likely. The state has supplemented the Clean Water Trust with additional state and federal funds in recent years, but current resources are not up to the challenge. An EBB provides a chance for the state to develop a coordinated plan to harness local, state and federal resources to tackle water infrastructure.