State of North Carolina

Debt Affordability Study

February 1, 2026

Debt Affordability Advisory Committee

Department of State Treasurer
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STATE OF NORTH CAROLINA
DEBT AFFORDABILITY ADVISORY COMMITTEE

February 1, 2026

To: Governor Josh Stein
Senator Phil Berger, President Pro Tempore of the North Carolina Senate
Representative Destin Hall, Speaker of the North Carolina House of Representatives
Fiscal Research Division, North Carolina General Assembly

Attached is the February 1, 2026, report of the Debt Affordability Advisory Committee, submitted pursuant to North Carolina G.S. 142-101. The report was created to serve as a tool for sound debt management practices by the State of North Carolina.

The report provides the Governor and General Assembly with a basis for assessing the impact of future debt issuance on the State's fiscal position and enables informed decision-making regarding both financing proposals and capital spending priorities. It also provides a methodology for measuring, monitoring and managing the State's debt levels, thereby protecting North Carolina’s bond ratings of AAA/Aaa/AAA (as rated by S&P, Moody’s, and Fitch, respectively). The Committee’s methodology (1) incorporates trends in debt levels and peer group comparisons and (2) provides recommendations within adopted guidelines. The analysis includes the projected issuance of all authorized but unissued debt.

The Committee recommends continuing the single target calculation it has recommended in prior years, advising that debt service and the continuing annual appropriation to the Solvency Fund should not exceed 4% of revenues.

I believe that this recommendation continues to represent action to preserve and protect the State’s triple triple-A rating.

Respectfully submitted,

Bradford B. Briner
State Treasurer of North Carolina
Chair, Debt Affordability Advisory Committee

Debt Affordability Advisory Committee Membership

Bradford B. Briner, State Treasurer, Chair

McKinley Wooten, Jr., Secretary of Revenue

Kristin Walker, State Budget Director

Dave Boliek, State Auditor

Nels Roseland, State Controller

Frank H. Aikmus, Senate President Pro Tempore Appointee

Greg Spaniolo, Senate President Pro Tempore Appointee

Eugene W. “Gene” Chianelli, Jr., Speaker of the House Appointee

Donald G. Pomeroy II, Speaker of the House Appointee

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SUMMARY

Background and Context

A study of debt affordability is an essential management tool that provides a comprehensive assessment of a government's ability to issue debt for its capital needs. S&P Global Ratings ("S&P"), one of the three major bond rating agencies, has stated that *"Most of the 'AAA' states have a clearly articulated debt management policy. Evaluating the impact of new or authorized but unissued bond programs on future operating budgets as well as unfunded liabilities are an important element of debt management and assessing debt affordability."* Control of debt burden is a key factor used by rating agencies' analysts in assessing credit quality.

G.S. 142-101 requires the Debt Affordability Advisory Committee (the "Committee" or "DAAC") to annually advise the Governor and the General Assembly of the estimated debt capacity of the General, Highway and Highway Trust Funds for the upcoming ten fiscal years. The statute also directs the Committee to recommend other debt management policies it considers desirable and consistent with the sound management of the State's debt. The Committee hereby presents its study (the "Study") for 2026.

Debt Controls

Debt capacity is a finite resource. This Study helps the State plan future debt issuances within current and projected future resource limits by comparing the State's current debt position to relevant industry and peer benchmarks. It serves as a tool for shaping and implementing the State's capital budget and is premised on the concept that resources — not only needs — should guide the State's debt issuance program.

The Committee's adopted guidelines attempt to balance two priorities:

- Providing sufficient debt capacity to allow for the funding of essential capital projects.
- Maintaining fiscal discipline to avoid jeopardizing future budgetary flexibility or the State's strong credit position.

The Committee has adopted "debt service as a percentage of revenues" as the controlling metric to determine the State's debt capacity. Over the ten-year planning horizon, the Committee's General Fund revenue projections show a positive trend, but weakening due to uncertainties across sectors and other conditions not excessively impacted from earlier declines in economic activity or recent volatility in interest rates. Debt service projections incorporate the future issuance of $1.1 billion of Build NC Bonds.

The General Fund model results indicate that the State's General Fund has debt capacity of approximately $1.93 billion in each of the next 10 years, or up to approximately $11.68 billion in the first year.

The Transportation model results indicate transportation debt capacity of approximately $155 million in each of the next 10 years, or approximately $920.2 million in the first year. (See Section II: Transportation Debt Affordability – project funding is not projected to be significantly curtailed.) Absent any future authorizations, Transportation debt service as a percentage of Transportation revenues peaks at 5.02% in FY 2030.

Refunding & Early Redemption Opportunities

Over the past ten fiscal years, the State has refunded approximately $2.5 billion of outstanding debt, achieving budgetary savings of over $239 million. In October and November 2025, the State refunded $480.5 million in Limited Obligation Bonds and General Obligation Bonds and tendered a portion of callable bonds. These transactions resulted in savings of $23.1 million, representing 3.05% of par and a reduction of overall debt and debt service payments.

Interest Rate Levels

The 10-year benchmark Treasury closed at 4.16% on December 31, 2025. This is below the long-term average rate of 4.25%. Major changes to interest rates that would significantly affect the State's capacity calculations remain unlikely.

Other Recommendations
(See Appendix A for further discussion)

- **Maintain Centralized Control of Debt Authorization Authority and Management**
  One of North Carolina's credit strengths is its centralized approach to debt authorization, issuance, and management. The Committee believes that decisions about prioritizing capital projects and issuing obligations — or entering into financial arrangements that create debt or debt-like obligations that increase the State's debt burden — should remain the exclusive responsibility of the General Assembly.

- **Maintain Structural Budget Balance and Continue to Replenish Reserves**
  Structural budget balance and the replenishment of reserve should continue to be a priority of the State. These are key drivers contributing to the State's "AAA" rating.

- **Consider General Obligation Bonds as the Preferred Financing Vehicle**
  General Obligation ("GO") Bonds generally approved by voters should be the preferred, but not exclusive, financing vehicle to fund the State's capital projects. There is an incremental cost when issuing debt other than GO Bonds. Depending upon market conditions, additional credit support and structure, the financial markets usually assess an interest rate penalty of 5-25 basis points for the State's appropriation-supported debt when compared with the State's GO bonds.

SECTION I: GENERAL FUND DEBT AFFORDABILITY

The State's outstanding debt position as of June 30, 2025, is detailed below.

State of North Carolina Outstanding Net Tax-Supported Debt

The State's outstanding debt at June 30, 2025, totaled approximately $7.38 billion, of which $4.06 billion was tax-supported.

Tax-Supported	**Amounts ($ millions)**
General Obligation Debt	$1,412.6
General Fund ($1,412.6)	
Highway Fund ($0)	
Special Indebtedness	$1,978.9
General Fund ($695.0)	
Highway Fund ($1,283.9)	
NCTA Gap-Funded Appropriation Bonds	$660.7
Other Debt-like Obligations	$7.4
Total General Fund Tax-Supported Debt	$2,775.7
Total Highway Tax-Supported Debt	$1,283.9
Subtotal, Tax-Supported Debt	**$4,059.6**
Non-Tax Supported	
GARVEE	$1,044.6
NC Turnpike Authority (includes TIFIA)	$2,161.9
Guaranteed Energy Savings Contracts	$115.4
Total State of North Carolina Debt	**$7,381.5**

Trends in Amounts of General Fund Debt

The State's outstanding net tax-supported General Fund debt was approximately $2.78 billion on June 30, 2025. Absent additional authorizations, the absolute level of General Fund tax-supported debt is not projected to exceed approximately $1.93 billion over the projection period and will decline by approximately 85% over the next 10 years. As of December 31, 2025, the State had no General Fund authorized but unissued tax-supported debt.

Debt Service

General Fund debt service will total approximately $357 million in FY 2026. Debt service continues to decline both in absolute dollars and as a percentage of revenue. Assuming no future authorizations, General Fund debt service will conclude by June 30, 2039.

Review of State Credit Ratings and Comparative Ratios

Credit ratings are the rating agencies' assessment of a governmental entity's ability and willingness to repay debt on a timely basis. As a barometer of financial stress, credit ratings are an important factor in the public credit markets and can influence the interest rates a borrower must pay.

The State's general obligation bonds have the highest ratings attainable from the three major rating agencies (i.e., AAA with a "stable" outlook by Fitch and S&P and Aaa with a "stable" outlook by Moody's Investors Service). North Carolina has a long history of AAA ratings on the State's general obligation bonds and is well positioned to weather future economic downturns. In 2025 rating reports, rating agencies identified the following factors that could lead to a downgrade or downward rating pressure:

- Tax cuts leading to operating deficits that pull available fund balance below 15% on a sustained basis.
- Economic slowdown causing material fiscal strain.
- Significant difficulty passing budgets or other fiscal governance weakening.
- Misalignment of revenue with expenditure growth.

Comparison of Debt Ratios to Selected Medians

The following table compares North Carolina to thirteen peer group states rated "triple-A" by all three credit rating agencies (often termed "triple triple-A" or "AAA"); this analysis combines General Fund and Transportation tax-supported debt. Our peer states are of a diverse nature, but all demonstrate adherence to certain underlying core values including prudent use (in some cases, extremely modest use) of debt. As shown, the State's debt ratios are at or below the median levels among the peer group.

North Carolina Net Tax-Supported Comparative Debt Ratios (1)

State	Debt to Personal Income % (1)	Debt per Capita (1)	Debt as % of GDP (1)	Debt Service Ratio (2)
Indiana (3)	0.50%	334	0.40%	0.59%
Iowa (3)	0.50%	349	0.40%	0.63%
Tennessee	0.50%	312	0.40%	0.45%
Missouri	0.60%	382	0.50%	0.88%
South Dakota (3)	0.70%	525	0.60%	1.01%
Florida	0.90%	609	0.80%	1.41%
North Carolina	0.90%	552	0.70%	1.10%
Texas	0.90%	610	0.70%	1.13%
Utah	0.90%	573	0.70%	0.98%
Georgia	1.70%	1,046	1.30%	2.16%
Minnesota	2.10%	1,573	1.80%	1.53%
Ohio	2.30%	1,446	1.90%	2.91%
Virginia	2.60%	2,036	2.40%	2.67%
Delaware	6.50%	4,479	4.20%	3.58%
Peer Group Median	0.90%	591	0.70%	1.11%

(1) Source: Moody's Investor Services; Moody's Financial Ratio Analysis
(2) Source: S&P report dated October 23, 2024, defined as debt service as a % of general fund spending.
(3) Implied by all three rating agencies; have not issued GO debt.

General Fund Guidelines, Debt Affordability Model and Results

General Fund Debt Capacity Recommendations

The Committee recommends the following two guidelines:

1. Net Tax-Supported Debt Service as a percentage of general tax revenues should be targeted at no more than 4.00% and should not exceed 4.75%; and

2. Net Tax-Supported Debt as a percentage of Personal Income should be targeted at no more than 2.5% and should not exceed 3.0%

Model Solution

The following table illustrates the amount of new tax-supported debt that could be authorized and issued, by year, using the 4% debt service to revenue target ratio.

General Fund Debt Capacity Using 4% Debt Service to Revenue Target Ratio

($ in Millions)

Fiscal Year	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030
Total Additional Debt Capacity per year*	$11,684.6	$99.85	$378.4	$970.12	$803.49
Debt Capacity available each and every year	$1,930.0	$1,930.0	$1,930.0	$1,930.0	$1,930.0

* In addition to that already authorized but unissued. Assumes additional debt capacity is authorized and issued in stated fiscal year

The following table illustrates the State's net tax-supported debt as a percentage of personal income; as shown, North Carolina has remained below the 2.5% target.

General Fund Debt to Personal Income Ratio

FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
0.15%	0.14%	0.12%	0.11%	0.10%	0.09%	0.06%

<u>General Fund Analysis – Other Commitments</u>

Pension and OPEB Unfunded Liabilities

The primary pension and Other Post-Employment Benefits (OPEB) plans covering North Carolina's teachers and state employees have unfunded liabilities totaling $33.6 billion, as reported in North Carolina's 2025 Annual Comprehensive Financial Report ("ACFR"). On a funding basis, the combined total of the State's actuarially determined pension and OPEB contributions are in excess of 17% of the General Fund budget

<u>Teachers' and State Employees' Retirement System ("TSERS")</u>

The State has fully funded the Annual Required Contributions ("ARC") for the TSERS in 83 of the last 84 years, and the Net Pension Liability is $11.8 billion as reported in the 2025 ACFR. For the fiscal year ending in 2026, the Actuarially Determined Employer Contribution ("ADEC") is approximately $3.2 billion

During 2018, the plan's discount rate (i.e., assumed rate of return) was reduced from 7.20% to 7.00%. In early 2021, the discount rate was further reduced from 7.00% to 6.50% as recommended by a regular experience review conducted by the plan's independent consulting actuaries.

OPEB

The State's OPEB plan covers retiree healthcare costs administered by the State and funded through the Retiree Health Benefit Fund ("RHBF"). As reported in the 2025 ACFR, the State's Net OPEB Liability ("NOL") was $22.0 billion, a 35% decrease from the prior year. The Actuarially Determined Employer Contribution is estimated to be $1.73 billion. The funding ratio for the RHBF (the ratio of assets to the liability) increased to 16.2%, compared to 9.8% last year.

An Employee Benefit Trust Fund (the "Solvency Fund") has been established to augment the assets of the RHBF (see Appendix D.) S.L. 2021-180 allocated $40 million to the Solvency Fund for Fiscal Year 2022 and $10 million for Fiscal Year 2023. The General Assembly adjusted the percentage of salary to the RHBF in FY 2023 to account for the $40 million drafted in FY 2022. The FY 2024 percentage of salary contributions accounted for the remaining $10 million. Session Law 2023-134 modified the allocation of the Solvency Fund to go 100% to the RHBF instead of shared with the TSERS fund. Effective FY 2024, all funds in the Unfunded Solvency Reserve Fund will go toward the Retiree Health Benefit Trust in an effort to address OPEB liabilities.

Level of Reserves

The State ended FY 2025 with a positive fund balance in the General Fund of approximately $21.1 billion as calculated under generally accepted accounting principles ("GAAP"). The Savings Reserve ("Rainy Day Fund"), which is part of the General Fund fund balance, was reported at $3.62 billion in the FY 2025 ACFR.

S.L. 2022-74 established the Stabilization and Inflation Reserve to make appropriated funds available for costs associated with inflation and other measures necessary to stabilize the State economy. The Stabilization and Inflation Reserve had a balance of $1.0 billion on June 30, 2025.

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SECTION II: TRANSPORTATION DEBT AFFORDABILITY

Review of Transportation Funds, Debt and Other Commitments

North Carolina funds transportation expenditures out of two major funds — the Highway Fund and the Highway Trust Fund — which operate closely together to support Department of Transportation ("DOT") activities.

> **The Highway Fund:** The Highway Fund accounts for most DOT activities including the construction and maintenance of the State's primary and secondary road systems, the Division of Motor Vehicles, transit, aviation, rail and ferry system. The primary revenue sources are federal funds, motor fuels taxes (75%), vehicle registration fees, and driver's license fees.
>
> **The Highway Trust Fund ("HTF"):** The Highway Trust Fund was established to provide a dedicated funding mechanism to meet specific highway construction needs in North Carolina. It is the only source of repayment for the Build NC bonds; thus, actions which diminish the HTF's resources have the potential to impair the ratings of the Build NC program. The principal revenue sources are highway use taxes, motor fuels taxes (25%) and various fees.

The two funds are in many ways managed as a combined entity as interfund transfers occur on a routine basis. Due to their interdependent nature, the Committee finds it most useful to calculate the available debt capacities of these funds (collectively "Transportation Funds") on an aggregate basis. The resulting debt capacity is termed the "Transportation debt capacity."

Transportation Debt

Highway Debt
The State has no current GO debt outstanding related to transportation projects

Build NC Bonds
The Build NC Bond Act of 2018 (S.L. 2018-16) authorized the issuance of bonds for regional and divisional transportation projects contained in the Statewide Transportation Improvement Plan. As of June 30, 2025, the State had issued $1.9 billion of the authorized $3.0 billion in bonds.

Debt Service on Transportation Debt
As the Build NC Bonds are issued, debt service supported by the Transportation Funds will increase to nearly $324 million in FY 2031. As discussed in more detail in Appendix C, appropriation of funds to support debt obligations under the Build NC Bonds, bonds issued by the North Carolina Turnpike Authority and any "availability payments" or other long-term contractual arrangements that support Public Private Partnerships ("P3") projects or similar arrangements are treated the same as any other debt service obligation. This is consistent with rating agency treatment

Other Commitments

Grant Anticipation Revenue Vehicle Bonds ("GARVEEs")
GARVEEs are a revenue bond-type debt instrument whose debt service is paid solely from future federal transportation revenues, with no State support. (G.S. 136-18(12b) as codified by S.L. 2005-

403 (“the GARVEE Act”)). GARVEEs represent a financing vehicle that provides significant funds to the State to accelerate transportation improvement projects. Because the program is not supported by state revenue, GARVEEs are not part of the Transportation debt affordability model

The State has issued multiple series of GARVEEs and the outstanding amount on December 31, 2025, was $1.04 billion. The NC GARVEE ratings assigned by Moody’s and S&P, are, respectively: Aa3/AA.

A GARVEE issuance occurred in April 2025.

North Carolina Turnpike Authority

North Carolina Turnpike Authority (“NCTA”) as a part of the Department of Transportation is authorized to construct and operate toll roads within the State and to issue revenue bonds to finance the costs. The General Assembly has authorized funding to “pay debt service or related financing costs” for various series of revenue bonds issued by the NCTA (called “gap funding”).

Transportation Debt Guidelines, Affordability Model and Results

The rating agencies consider all debt supported by statewide, generally applied taxes and/or user fees to be “Tax-Supported Debt.” This combined treatment extends to all General Fund-supported, and to Highway Fund and Highway Trust Fund-supported (“Transportation Funds”) debt. Some ratings analysts apply the same treatment to debt supported by non-State revenues such as GARVEE bonds. The Committee recognizes that the rating agencies compare the State to its peers using a broad measure of Transportation and General Fund debt and has reviewed the State’s relative status on this basis.

However, the State of North Carolina has a long history of viewing the debt supported by the General Fund as tax-supported debt and its Highway Bonds as being non-tax supported (in this case, Highway Trust Fund-supported) debt. The State’s existing debt affordability model excludes both transportation revenues and transportation debt service as components of the General Fund calculation. Continuing this practice, the Committee has determined that it should adopt a measure of Highway Fund and Highway Trust Fund debt capacity that is separate and distinct from that calculated for the General Fund. Although not common, this practice has been discussed with the rating agencies who understand North Carolina’s incremental and separate approach to debt affordability measurement.

The Committee also recognizes the inherent differences between the General Fund and the Transportation Funds, not only in terms of the revenue streams, but also in terms of the commitments on those revenues. In addition, the State’s transportation “enterprise” is, by its nature, a long-lived, capital intensive, rapidly growing program. As such, a customized individual debt capacity model is appropriate to measure the debt capacities of the Transportation Funds and the Committee believes that an individual Transportation debt capacity calculation is consistent with the legislative intent of S.L. 2007-551.

Due to the interdependent nature of the Highway and Highway Trust Funds as discussed earlier, the Committee has determined that it is more useful to calculate the available debt capacities of these Funds on an aggregate, rather than individual, basis. The resulting debt capacity is termed the “Transportation” debt capacity.

The Committee has adopted annual transportation-related debt service as a percentage of State transportation revenues as the measure to evaluate the level of Transportation debt capacity. By measuring the portion of the State's transportation resources committed to debt-related fixed costs, this ratio reflects the flexibility to allocate transportation resources to other priorities.

Revenues Used in the Transportation Model Calculation
The model uses a definition of State transportation revenues that includes an aggregate of all State-level revenues deposited into the Highway Fund and the Highway Trust Fund, including the motor fuels tax, highway use tax, motor vehicle license tax, sales and use tax and certain non-tax revenue such as investment income. Consistent with the model mechanics for the General Fund, there is no deduction for projected transfers to the General Fund, Powell Bill transfers or other non-debt commitments. Federal transportation revenues are specifically excluded from the definition of revenues used to calculate Transportation debt capacity as federal revenues have been pledged to the State's GARVEE program and are not available to back other transportation-related debt.

Debt Used in the Transportation Model Calculation
The model uses a definition of State transportation debt service that includes Build NC Bonds, Highway GO Bonds, gap funding, availability payments and other long-term contractual payments to support P3 or other structures but excludes the GARVEEs supported by federal revenues. There are currently no tax-supported capital lease obligations that need to be included. Highway Trust Fund support for debt issued by the North Carolina Turnpike Authority is included as a liability for model purposes.

Debt Structuring Assumptions
The standard calculation of the Transportation debt affordability model assumes that model debt is fixed-rate 25-year maturity debt with an average interest cost of 6.15% and a level debt service profile after the first year. This year, the Build NC Bonds were loaded into the model with the following assumptions:

- Fixed rate debt issued at 4%
- Level debt service after the first year
- 15-year final maturity
  $300 million issued in FY 2026 forward (Build NC Bond Act (as amended) expires 12/31/2031).

Transportation Debt Capacity Guidelines
The Committee has adopted a guideline of 6% for transportation-related debt service as a percentage of state transportation revenues. In doing so, the Committee determined that the Transportation Funds enjoy a greater degree of budgetary flexibility than the General Fund does, and the Committee determined that the State's Transportation funds could support a higher ongoing level of debt service as a percentage of revenues than was deemed appropriate for the General Fund. However, the Committee also determined not to adopt the same 20% guideline (S.L. 2020-91, s. 4.5(a) increased from 15% to 20%) for Transportation debt capacity as was contained in the GARVEE legislation because GARVEEs have higher annual debt service requirements due to their shorter maturity.

Transportation

Net Tax-Supported Debt Capacity using 6.0% debt service/revenues target ratio
(In millions of dollars)

Fiscal Year	2026	2027	2028	2029	2030
Total Additional Debt Capacity per Year*	$920.2	$0.0	$0.0	$0.0	$48.1
Debt Capacity Available each and every Year	$155.0	$155.0	$155.0	$155.0	$155.0

* In addition to that already authorized but unissued. Assumes additional debt capacity is authorized and issued in stated fiscal year
GAP Funding for North Carolina Turnpike Authority projects assumed to total $49 million annually.

Model Assumptions regarding Revenue Growth

The model uses consensus estimates for the revenues over the model horizon (see Appendix C).

SECTION III: Transportation and General Fund Ratios Combined

The Committee adopted the 6% Transportation guideline after analyzing the State's position relative to its peer group on an aggregate basis (i.e., with the General Fund and Transportation Funds combined), consistent with rating agency practice. Illustrated below is how the State appears on a combined basis using debt service as a percentage of revenue for both the General Fund and the Transportation Funds. The Committee notes that the combined ratio is projected to decline through FY 2030.

General Fund and Transportation Funds
Combined Debt Service / Revenue Percentages

	General Fund	Transportation (1)	Combined
2026	1.05%	3.45%	1.39%
2027	1.04%	3.78%	1.45%
2028	0.91%	4.19%	1.40%
2029	0.78%	4.49%	1.31%
2030	0.58%	4.83%	1.23%

Note: Percentages are based on forecasted revenues and debt service

(1) GAP Funding for North Carolina Turnpike Authority projects assumed to total $49 million annually.

Appendix A
Other Recommendations

1. **Policy Recommendation regarding continuing a 4% calculation target for General Fund Debt capacity**
   The Committee recommends that the 4% of revenues be continued as the targeted limitation for debt capacity. Under this policy, the amount of available debt capacity is significant, totaling approximately $1.93 billion per year for the next 10 years.

2. **Control of Debt Authorization Authority**
   The Committee continues to strongly recommend that the State of North Carolina maintain its historically conservative debt management practices with regard to (1) centralized debt authorization, (2) centralized debt management and issuance and (3) classification of debt and debt-like obligations when determining the debt burden. These practices are among those considered by the rating agencies when assigning their "triple-A" ratings to the State and ultimately allow the State to maintain a healthy financial position.

3. **Consider General Obligation Bonds as the preferred financing method**
   The Committee notes that the State has recently relied extensively, although not exclusively, on the authorization of Special Indebtedness to finance capital projects. Due to the potential debt service savings and increased transparency, the Committee believes that General Obligation bonds should be considered the preferred, but not the exclusive, method to debt finance the State's capital needs.

4. **Structural Budget Balance and Reserve Replenishment**
   The Committee confirms its view that North Carolina's priorities of achieving structural budgetary balance and maintaining healthy reserve fund balances are strong evidence of financial stability and flexibility. The Committee recognizes that long term budgetary stability and adequate reserve funds are key factors in maintaining our triple triple-A bond rating. The Committee further recognizes the following critical issues that were recently noted and will be monitored by bond rating agencies:

   - Adequate reserves must be maintained to address economic downturns.
   - Ensuring operating revenues and tax rates are sustainable and align with expenditures.
   - Timely budgets and sound fiscal governance are essential moving forward.

Appendix B

General Fund Revenues and Liabilities and Debt Affordability Model 10-Year Solutions

DAAC Revenues

The model uses general tax revenues adjusted for one-time or non-recurring items, statutory transfers to the Savings Reserve Fund ("Rainy Day Fund") plus certain investment income and miscellaneous revenues ("DAAC Revenues"). The Office of State Budget and Management ("OSBM") and Fiscal Research Division ("FRD") have been consulted to provide consensus projections through FY 2035.

General tax revenues adjusted for one-time or non-recurring items plus certain other revenue items deemed available to service debt from the most recently available *Annual Comprehensive Financial Report.* The following items are included:

General Fund Tax Revenues

- Individual Income Tax
- Corporate Income Tax
- Sales & Use Tax
- Franchise Tax
- Insurance Tax
- Beverage Tax
- Tobacco Products Tax
- Other Taxes

Other General Fund Revenue Items

- Investment Income
- Miscellaneous Revenues

Revenue Growth and Other Assumptions

The 10-year General Fund revenue projections start with certified revenues for Fiscal Year 2026; future years are projected based on forecasts from OSBM. OSBM's revenue projections are based on revenue collections and economic forecasts as of early January 2026 and do not incorporate direct or indirect effects of potential changes to federal policies. OSBM's revenue projections have historically been conservative, helping the state avoid exceeding recommended debt capacity.

The average projected growth rate for General Fund revenue, after any statutory transfers to the Savings Reserve or Unfunded Liability Solvency Reserve, over the next ten years is 2.1%, with an average growth rate of 0.4% between FY 2025 and FY 2030 and 3.8% between FY 2030 and FY 2035. This pattern reflects the fiscal impact of S.L. 2023-134, Sec. 42.1, which reduced the individual income tax rate to 4.25% in 2025 and 3.99% in 2026. The legislation also includes up to three additional 0.5% reductions in the individual income tax rate that are contingent upon revenue collections exceeding statutory thresholds (also known as triggers), potentially lowering it to a minimum of 2.49%.

The timing and number of tax rate reductions are sensitive to small changes in revenue projections and may differ significantly from current projections.

Additionally, S.L. 2021-180 reduces the corporate income tax rate gradually from 2.5% in 2024 to 0% in 2030. These tax rate reductions, combined with projected growth in the general economy, result in little revenue growth through FY 2030. Stable tax policy after 2030 results in stronger revenue growth between FY 2030 and FY 2035.

In consultation with OSBM and FRD, DAAC consensus revenue projections are:

General Fund Revenue Used in Debt Affordability Model[1]

($ millions)

Fiscal Year		Revenues ($ millions)	Growth Rate		Fiscal Year	Revenues ($ millions)	Growth Rate
2025		$33,954.0	2.6%		**2031**	$ 35,891.0	3.4%
2026		34,086.7	0.4%		**2032**	37,476.1	4.4%
2027		33,241.3	-2.5%		**2033**	39,051.7	4.2%
2028		33,065.7	-0.5%		**2034**	40,759.3	4.4%
2029		33,707.4	1.9%		**2035**	42,417.1	4.1%
2030		34,700.3	2.9%		**2036**	44,112.6	4.0%

* General Fund recurring tax revenues, miscellaneous revenues and Treasurer's investments per OSBM/FRD

[1] Fiscal Years 2026 - 2036 revenue forecast as of January 2026. Fiscal Year 2025 is budgetary actual.

<u>Liabilities Used in the General Fund Model Calculation</u>

The model uses a definition of net tax-supported debt that includes all outstanding and authorized, but unissued, GO Bonds, Special Indebtedness, and other debt like obligations that are owed to a third party over a predetermined schedule payable from General Fund tax revenues. Excluded are obligations of Component Units, Transportation debt actually paid from Transportation revenues, unfunded amounts in the Pension Plans, Employment Security borrowings, OPEB liabilities, and Energy Performance Contracts. Mandatory payments due to contractors or others under P3s, "Design/Build/Finance" or other such arrangements would be included as a liability for the model.

To calculate net tax-supported debt, credit analysts take into account all debt supported by general tax revenues. This debt position shows the amount of indebtedness serviced from an issuer's General Fund; that is, it reflects the debt service payments made directly from tax revenues and is known as net tax-supported debt. Although a consensus appears to exist among credit analysts as to the appropriateness of using net tax-supported debt as the standard for determining an issuer's debt position, there is less unanimity about the precise calculation. The Committee has determined to exclude self-supporting debt from its calculations.

The model includes the actual debt service from all outstanding net tax-supported debt and for all authorized, but currently unissued, tax-supported debt if such issuance does not require further action on the part of the General Assembly.

The following is a list of those liabilities that are included in the General Fund model (outstanding amounts as of June 30, 2025, unless otherwise noted):

- GO Bonds supported by General Fund Tax Revenue - $1,412.6 billion
- General Fund appropriation-supported debt
    - Limited Obligation Bonds - $695 million
    - Other debt like obligations - $7.4 million

Liabilities not included in the General Fund model (outstanding amounts as of June 30, 2025):

- $ 22.0 billion OPEB
- $ 24.2 billion Obligations of the University of North Carolina System, Community Colleges, State Health Plan and other Component Units
- $ 11.8 billion Pension liabilities
- $ 1.1 billion Highway Construction Special Indebtedness supported by the Highway Trust Fund (as of 6/30/2024)
- $115.4 million Energy Performance Contract obligations where such obligations are guaranteed and approved pursuant to G.S. 142-64 and not supported by separate appropriations ($310.0 million issued)

Note: Although these liabilities may not constitute tax-supported debt, some are obligations of the State or various component units and the State's General Fund, although not legally obligated to, could be called upon to service these obligations if necessary.

Debt Structuring Assumptions

The General Fund model uses a standard fixed-rate 20-year level principal or payment structure and the following assumptions in this year's debt affordability model calculations:

- The State does not have any outstanding Variable Rate Debt and is not expected to issue any over the model horizon.
- The State does not currently have any General Fund authorized but unissued GO or non-GO debt.
- Incremental model debt will be structured with a fixed rate 20-year maturity, a 6% interest rate, and an overall level debt service profile after the initial year.

Note on Interest Rate Assumptions

The DAAC model assumes consistency between the issuing assumptions used in the study and those used for budgetary planning. The issuance of future authorized bonds could be at lower rates than those stated above, especially in the early years. Such savings are not expected to significantly impact the results of the Study.

General Fund: 10-Year Model Solutions

The following table compares the General Fund debt capacity using both 4.0% and 4.75% debt service to revenue ratios.

General Fund Debt Capacity Comparison
($ in Millions)

	Using 4% Target Ratio of Debt Service to Revenue		Using 4.75% Ratio of Debt Service to Revenue	
	Additional Capacity Per Year	Total Capacity Available Per Year	Additional Capacity Per Year	Total Capacity Available Per Year
FY 2026	$11,684.6	$1,930.0	$ 14,616.9	$2,285.0
FY 2027	$99.8	$1,930.0	$ 27.1	$2,285.0
FY 2028	$378.4	$1,930.0	$363.3	$2,285.0
FY 2029	$970.1	$1,930.0	$1,025.3	$2,285.0
FY 2030	$803.5	$1,930.0	$888.9	$2,285.0
FY 2031	$1,018.9	$1,930.0	$1,121.3	$2,285.0
FY 2032	$1,005.6	$1,930.0	$1,142.0	$2,285.0
FY 2033	$879.4	$1,930.0	$1,014.9	$2,285.0
FY 2034	$813.1	$1,930.0	$ 960.0	$2,285.0
FY 2035	$907.4	$1,930.0	$1,050.1	$2,285.0

* In addition to that already authorized but unissued. Assumes additional debt capacity is authorized and issued in stated fiscal year.

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Appendix C

Transportation Revenues and Liabilities and Debt Affordability Model 10-Year Solutions

State Transportation Revenues

The Transportation debt affordability model uses all state transportation revenues plus other revenue items (excluding Federal Transportation Revenues) deemed available to service debt for the most recent fiscal year. The following items are included:

- Motor Fuels Tax
- Highway Use Tax
- Motor Vehicle Revenues
    - Vehicle registration and title fees
    - Driver's license fees
    - International registration plan fees
    - Penalties
    - Equipment inspection fees
    - Other
- Investment Income
- Sales & Use Tax allocation
- Other miscellaneous revenue

Revenue Growth

The Office of State Budget and Management (OSBM) and the General Assembly's Fiscal Research Division (FRD), in conjunction with the North Carolina Department of Transportation (DOT), issued a consensus revenue forecast for the Highway Fund and Highway Trust Fund in May 2025. The projections include certified revenues for FY 2025, based on OSBM-FRD consensus projections, and joint DOT-OSBM projections for all subsequent years. Under the forecast, combined Highway Fund and Highway Trust Fund revenues grow 1.0% in FY 2026 and 1.4% in FY 2027. The result is higher-than-usual uncertainty in the 10-year revenue forecast, particularly in the late 2020s and 2030s.

Beginning in FY 2023, a portion of State's Sales and Use Tax revenue proceeds is transferred monthly to the Highway Fund and Highway Trust Fund, per G.S. 105-164.44M(b).

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The following table shows the estimated Sales and Use Tax transfers through FY 2036.

Estimated Sales and Use Tax Transfers to Transportation Funds
($ in Millions)

	Highway Fund	Highway Trust Fund	Total Transfer
FY 2026	$170.7	$512.1	$ 682.8
FY 2027	$176.2	$528.4	$ 704.6
FY 2028	$181.8	$545.6	$727.4
FY 2029	$188.2	$564.6	$752.8
FY 2030	$195.2	$585.7	$780.9
FY 2031	$201.9	$605.7	$807.6
FY 2032	$208.8	$626.2	$835.0
FY 2033	$216.1	$648.3	$864.4
FY 2034	$223.5	$670.7	$ 894.2
FY 2035	$231.3	$693.8	$925.1
FY 2036	$239.3	$717.9	$957.2

Transportation Revenue
($ millions)

	Revenues	Growth Rate			Revenues	Growth Rate
FY 2025	$5,707.2	9.8%		**FY 2031**	$ 6,362.3	1.8%
FY 2026	5,764.5	1.0%		**FY 2032**	6,472.7	1.7%
FY 2027	5,847.1	1.4%		**FY 2033**	6,678.0	3.2%
FY 2028	5,924.4	1.3%		**FY 2034**	6,803.6	1.9%
FY 2029	6,124.0	3.4%		**FY 2035**	6,919.1	1.7%
FY 2030	6,247.3	2.0%		**FY 2036**	7,045.4	1.8%

* Revenue amounts per transportation consensus forecast (OSBM, FRD & DOT). Fiscal Year 2025 is budgetary actual. Includes Sales & Use Tax transfer projections.

<u>Transportation Liabilities</u>

The model uses the debt service from all outstanding and authorized but unissued Highway Bonds (i.e., both GO and Build NC Bonds) and includes transportation-related and installment purchase contracts if appropriate. Debt service arising from the State's GARVEE program is not included as a State Transportation Liability because GARVEEs are supported solely by federal transportation revenues.

The General Assembly has authorized funding to "pay debt service or related financing costs" for various series of revenue bonds issued by the North Carolina Turnpike Authority. The funds so appropriated are legally pledged to support the bonds and bondholders will depend upon the appropriations continuing. Therefore, the model treats the gap funding as the equivalent of debt service because it represents ongoing Highway Trust Fund support of debt. $49 million of gap funding is treated as debt service for each year over the 10-year model horizon. DOT has also pledged certain operating and maintenance funds to secure debt, if necessary, to provide adequate coverage levels. At present, it appears that such funding will not be required. However, these funds would be treated as additional gap funding for model purposes if DOT were to be required to make such payments.

Availability Payments

The model counts "availability payments" as debt-like obligations. These payments are contractually owed to the contractor or other service provider on a delayed schedule that stretches beyond the standard construction period. Sometimes entered into as part of Public Private Design/Build/Finance and/or other arrangements, the delayed payments represent debt service for contractor-provided financing. The debt-like characteristics of availability payments (even if "subject to appropriation") mean that the payments are treated as a liability for the purposes of the model.

Debt Issuance Assumptions

The following assumptions were used in this year's Transportation debt affordability model calculations because the Build NC Bonds have specific structuring limitations, and their issuance utilizes all of the available Transportation debt capacity:

- There is no remaining authorized but unissued highway GO debt and $1.1 billion of authorized but unissued non-GO Build NC bonds on December 31, 2025.
- The Build NC Bonds will be structured with a fixed rate 15-year maturity, a 4.00% interest rate and an overall level debt service profile after the first year.

Transportation: 10-Year Model Solution

Transportation Net Tax-Supported Debt Capacity Using 6.0% Debt Service to Revenue Target Ratio

($ in Millions)

	Additional Capacity Per Year	Total Capacity Available Per Year
FY 2026	$920.2	$155.0
FY 2027	$0	$155.0
FY 2028	$0	$155.0
FY 2029	$0	$155.0
FY 2030	$48.1	$155.0
FY 2031	$83.5	$155.0
FY 2032	$155.2	$155.0
FY 2033	$95.0	$155.0
FY 2034	$87.3	$155.0
FY 2035	$450.7	$155.0

Appendix D

Review of Recent Debt-Related Legislation

Build NC Bond Act of 2018, G.S. § 142-97
S.L. 2018-16, s. 4; as amended by S.L. 2019-251; S.L. 2020-91; S.L. 2021-180; S.L. 2021-189; and S.L. 2024-15, ss. 9, 10 (a)-(c)

The Build NC Bond Act (the "Act") authorizes the issuance by the State Treasurer of up to $3 billion bonds for regional and divisional transportation projects contained in the Statewide Transportation Improvement Plan subject to a number of constraints including Council of State approval; cash balances, measured at specific times, that dip below $1 billion; a recommendation from the Treasurer that the Bonds be issued; an issuance limitation of no more than $300 million per year (the amount authorized to be issued in FY 2021 was increased to $700 million by S.L. 2020-91); and compliance with the limitations contained in the DAAC Study. The Bonds, authorized as Special Indebtedness, are also subject to the provisions of Chapter 142, Article 9 (the State Capital Facilities Finance Act).

The Act's authorization originally expired December 31, 2028. Session Law 2024-15, Sec. 9, extended the Act's authorization expiration date to December 31, 2031. The Bonds are to be paid by appropriations from the Highway Trust Fund. The bonds are limited to a 15-year final maturity.

State Pension/Retiree Health Benefit Fund Solvency, G.S. § 143C-4-10
S.L. 2018-30, Sec. 1; as amended by S.L. 2020-48, Sec. 2.2(a), (c); S.L. 2021-180, Sec. 39.24(a); and S.L. 2023-134, Sec. 39.28(a)

The legislation established the "Unfunded Liability Solvency Reserve" (the "Solvency Fund") as a reserve within the General Fund that will be used to accumulate funds to be used to reduce the State's unfunded pension and OPEB liabilities. To the extent that the Savings Reserve balance has reached its statutory maximum, the Solvency Fund will receive amounts that otherwise would have gone to the Savings Reserve. The Solvency Fund may also receive additional appropriations.

State Capital and Infrastructure Fund ("SCIF"), G.S. § 143C-4-3.1
S.L. 2017-57, Sec. 36.12(b); as amended by S.L. 2018-5, Sec. 36.8(a); S.L. 2020-81, Sec. 4(f); S.L. 2021-
180, ss. 5.7(a), 40.12; S.L. 2022-74, Sec. 40.3(a); S.L. 2023-134, Sec. 40.5(c)

Session Law 2017-57 established a fund to be used to address ongoing capital and infrastructure needs effective July 1, 2019. Monies in the SCIF are to be used to pay debt service (first priority) and then fund new capital projects and repair and renovation projects.

Transfer to Highway Fund, G.S. § 105-164.44M(b)
S.L. 2022-74, Sec. 42.3(a); as amended by S.L. 2024-15, Sec. 18(a)

A portion of sales tax revenues collected under G.S. § 105-164.44M(b) will be transferred to the Highway Fund and Highway Trust Fund, with the first such transfers having occurred in State Fiscal Year 2023. For State Fiscal Year 2025 and forward, 1.5% will be transferred to the Highway Fund and 4.5% will be transferred to the Highway Trust Fund.