F I S C A L   I M P A C T   R E P O R T

SPONSOR Campos **DATE TYPED** 2-13-04 **HB**

SHORT TITLE Earmarking Funds for Economic Development **SB** 457/aSCORC

ANALYST Neel

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY04	FY05			
		Indeterminate	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to:

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Treasurer's Office (STO)
Attorney General's Office (AGO)
Department of Finance and Administration (DFA)

SUMMARY

Synopsis of SCORC Amendment

The Senate Corporations and Transportation Committee amendment requires the Board of Finance to require 55 percent of state deposits in a bank, savings and loan association or credit union be used for stimulating economic development in the local community. Prior to the amendment, the BOF was given the option to require the investments in economic development.

Synopsis of Original Bill

Senate Bill 457 allows the state board of finance to require that a certain percentage of state deposits be used to stimulate economic development in communities associated with the particular bank, savings and loan association, or credit union.

Significant Issues

STO states that additional employees and the related personnel expenses will be incurred if the proposed language in SB 457 is enacted into law. The additional personnel would be required to accurately and effectively monitor the financial institution's compliance with the proposed language in this bill.

DFA reports the following:

The present State Treasurer's Investment Policy allows the State Treasurer to invest a maximum of $300 million in certificates of deposit (CDs) in state financial institutions, with a maximum limit of $30 million in any single financial institution. As of December 31, 2003, the total State Treasurer's portfolio available for investment was $4.5 billion. The amount invested in CDs was $220 million.

The State Board of Finance Interest Rate Policy on Public Funds sets the minimum interest rates financial institutions must pay for public funds deposits in CDs. Rates are based on the bond equivalent yield of the United States Treasuries of the closest maturity. Based on this policy, the minimum interest rates financial institutions must pay on State Treasurer's deposits for February 4, 2004 are: 6-month CD, 1.02%, 1-year CD, 1.16%, 2-year CD, 1.73% and a 3-year CD, 2.27%. With short-term interest rates at 40-year lows, financial institutions have access to low interest rate capital. Because of the low rates financial institutions pay on state deposits, they often "arbitrage" the funds in national securities markets to earn a higher yield than what they pay for the use of state funds, profiting by the interest rate spread. This practice improves the profitability of financial institutions, but doesn't benefit the local community where the financial institution is located. This legislation would require a portion of state funds on deposit in local financial institutions to be lent out in the community, based on guidelines established by the State Board of Finance.

In 2003, the State Board of Finance and State Treasurer agreed to increase the maximum level of CD deposits for the State Treasurer's portfolio from $200 million to $300 million and the maximum deposit level per individual financial institution from $20 million to $30 million. Additionally, they discussed requiring financial institutions receiving an amount over $20 million, up to the $30 million cap, to lend the money back out in the local community to stimulate the local economy. Legal counsel advised the State Board of Finance that imposing this requirement of lending money back into the community should be a statutory mandate instead of an administrative requirement done by rule or policy. Based on this advice, the State Treasurer's Investment policy was amended with language that "urged" banks to lend this money out in their respective local communities to spur economic development. The language in the investment policy is suggestive and not mandatory. Placing this requirement in statute would authorize the State Board of Finance to set requirements for financial institutions accepting state deposits to make loans in their respective communities for economic development purposes.

FISCAL IMPLICATIONS

Economic theory indicates that requiring a portion of the state's deposits in financial institutions be used for economic development would dilute the yield on STO's portfolio or increase the risk to the portfolio, thereby potentially impacting general fund revenues. However, it is difficult to quantify a fiscal impact until the state Board of Finance enacts policies to carryout SB 457.

SN/dm:lg