FISCAL IMPACT REPORT

		ORIGINAL DATE	2/6/18		
SPONSOR	Ely	**LAST UPDATED**		**HJM**	17
SHORT TITLE	Study Creating State Bank of NM			**SB**	
				ANALYST	Romero

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY18	FY19	FY20	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		NFI				

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
State Investment Council (SIC)
Regulation and Licensing Department (RLD)
Office of State Auditor (OSA)

SUMMARY

Synopsis of Bill

House Joint Memorial 17 requests the Legislative Council to form a task force to study the establishment of a state bank in New Mexico. The study would be completed and reported to the appropriate interim legislative committees by November 1, 2018.

FISCAL IMPLICATIONS

No fiscal impact.

SIGNIFICANT ISSUES

The Regulation and Licensing Department provided the following:

> "The FID suggests the following non-exclusive list of items/issues be included within any study conducted by the LC when evaluating the structure and processes of the possibility of a state-owned bank alongside current New Mexico law and sound banking practices:

- "Anti-Donation Clause" of the New Mexico Constitution:
  - The formation of a "bank" being owned/run by any unit of government within the State of New Mexico using public funds to finance the "bank" appears to be in

conflict with the language and intent of Article IX, Sect. 14 of the New Mexico State Constitution (commonly known as the "Anti-Donation Clause").

- Prior to the establishment/chartering of a bank in the State of New Mexico that would follow a structure similar to that of the State Bank of North Dakota, a state constitutional amendment would be required.

- How would a "state bank" in New Mexico be insured?
  - All New Mexico state chartered banks are required to be insured:
    - §58-1-2 NMSA 1978, (A) "bank" means: (1) an "insured bank" as defined in Section 3(h) of the Federal Deposit Insurance Act.
    - §58-1-61 NMSA 1978 "(B) Before actually transacting any banking business or accepting any deposits, the applicant must file with the commissioner [director] satisfactory proof showing that insurance of deposits has been obtained through the federal deposit insurance corporation or other appropriate agency or instrumentality of the United States government.
    - §58-1-70. Deposit insurance; membership in the Federal Reserve System. "A state bank shall obtain insurance of its deposits by the United States or any agency thereof, and may acquire and hold membership in the Federal Reserve System."

- Deposits/Protections:
  - Most banks are funded substantially through deposits. The state needs to consider the source of protection for those deposits. Traditional banks rely on deposit insurance coverage, subject to certain limits, from the Federal Deposit Insurance Corporation (FDIC).
  - The deposits of the Bank of North Dakota are not FDIC insured, but are guaranteed by the full faith and credit of the State of North Dakota.
  - In the FDIC's Statement of Policy for Applications for Deposit Insurance, the FDIC expresses its concern about institutions owned by domestic governmental units being controlled by the political process. Additionally, the FDIC notes, the institutions could raise special concerns relating to management stability, and the ability and willingness to raise capital.

- Oversight:
  - U.S. banks are actively supervised by chartering authorities, including the FID, the FDIC, the Federal Reserve, and/or the Office of the Comptroller of the Currency (OCC).
  - An independent regulator must also have the tools necessary to seek corrective measures through formal enforcement actions, civil money penalties, and removal of bank officers and directors.

- Safety & Soundness of the Bank:
  - Primary objectives of regulators should always be the safety & soundness of financial institutions, compliance with laws, regulations, and supervisory policy. This includes, but is not limited to:
    - Careful consideration should be given to the investment and lending authority of a state-owned bank in order to avoid risks to the solvency of the institution and prevent undue competition with privately owned banks. Appropriate limitations should be established on loans to insiders and

affiliated entities. There should also be limitations established on loans to one borrower or group of affiliated borrowers.

- One concern about a government-owned bank is the possibility of lending and other banking decisions to be affected by political concerns rather than strictly economic factors. For example, if the bank were to under-price risk on loans for new development projects due to the political popularity of such projects, the security and soundness of the bank could be jeopardized.

- Governance and Managerial Factors:
  - Corporate governance is a critical component for all banks. Ultimately, the board sets the policies of the bank, determines the desired risk profile, and oversees management.
  - One of the most important decisions for any financial institution is selecting the executive management team, since there is a direct relationship between the overall conditions of a bank, the quality of its management team, and the future performance of the bank.

- Capital Adequacy:
  - Banks need to be supported by monetary capital. The state will need to determine the source of this capital, recognizing the need for it to remain in the bank throughout its existence. Capital should be sufficient at inception to support anticipated start-up costs and expected growth. In addition, the state should make a provision for contingent capital should the bank experience unexpected losses, requiring recapitalization. Federal regulations require leverage capital to be greater than 5% for a bank to be considered "well capitalized." The term, "well capitalized," refers to a category under Prompt Corrective Action. Banks with capital below this category are subject to certain mandated regulatory restrictions. Banks generally find it necessary and desirable to hold significantly higher levels. The current industry average is just below 11%. By this standard, a bank projected to be $1 billion in assets, would need $110 million in capital, just to open its doors."

OTHER SUBSTANTIVE ISSUES

The State Investment Council provided the following:

> "The Legislative Council is identified as the entity in charge of selecting the majority of the members of the task force, but the bill is not explicit in how that process might work, and who might be in charge of selecting the individual members of the task force. The guidelines, "…ten members of the public with interest or expertise in financial issues…" are similarly not well defined. That may well be the intent, as it gives more latitude for those driving the process to get a broadly diversified group with a wide variety of perspectives and expertise. The converse however, can also apply, should the goals and conclusions of the task force be pre-ordained."

IR/sb