Date of Hearing: April 27, 2011

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT AND THE ECONOMY
V. Manuel Pérez, Chair
AB 750 (Hueso) – As Amended: April 25, 2011

SUBJECT: Investment Trust Blue Ribbon Task Force

SUMMARY: Establishes the Investment Trust Blue Ribbon Task Force for the purpose of considering the viability of establishing the California Investment Trust (Trust). Specifically, this bill:

1) Expresses legislative intent that among other things the Trust could serve to more effectively meet the financial needs of the state including:
   a) Supporting economic development by increasing access to capital for businesses in the state;
   b) Providing financing for housing development, public works infrastructure, educational infrastructure, student loans, and community quality of life projects;
   c) Providing for a more stable local financial sector;
   d) Reducing the cost paid by state government for banking services; and
   e) Lending capital to banks, credit unions, and nonprofit community development financial institutions to assist in meeting their goals of increasing access to capital and providing banking services.

2) Requires the Secretary of the Business, Transportation and Housing Agency (BTH) to convene an Investment Trust Blue Ribbon Task Force (Task Force) comprised of the following members:

   a) Five members appointed by the Governor;
   b) Two members appointed by the Senate Rules Committee;
   c) Two members appointed by the Speaker of the Assembly;
   d) The Governor or his designee;
   e) The State Controller or his designee;
   f) The State Treasurer or his designee; and
   g) The Secretary of BTH.

3) Requires that the first meeting of the Task Force be convened on or before February 1, 2012. The chair is to be chosen by the membership of the Task Force.

4) Provides that the purpose of the Trust is to consider the viability of establishing the Trust, which would serve as, among other things, a state bank receiving deposits of state funds, and to report to the Legislature on its findings and recommendations.

5) Provides that the Task Force shall consider one or more models for structuring the Trust. Among other issues to consider, the Task Force is directed to:

   a) Undertake a general assessment of the state's current network of public and private financial resources for the purpose of identifying potential areas of Trust focus;

   b) Consider the types of financial products that could be offered to address current unmet financial needs and/or more efficiently deliver financial resources and products;
   c) Examine various administrative and operational structures for organizing a Trust; and
   d) Consider options for integrating a state trust model into the existing state financial resource network.

6) Requires all expenses of the Task Force be paid from existing BTH resources. Travel expenses are limited to actual cost for appointed members.

7) Authorizes the Task Force to consult with stakeholders and establish an advisory committee. Advisory committee members are not entitled to expense reimbursement for their participation.

8) Requires the Task Force to submit a report by December 1, 2012 which does the following:

   a) Makes a recommendation on the viability of the Trust;

   b) Provides a list of findings based on the Task Force's review of the issues identified in number 5 above; and

   c) To the extent that the recommendation is supportive of the establishment of the Trust, identifies next steps toward creation of the Trust, including recommendations on the following:

      i) The administrative structure of the Trust;
      ii) The capital requirements for the Trust's initial capitalization and ongoing expenses;
      iii) How the initial capitalization and ongoing operating expenses could be funded;
      iv) The oversight of the operations of the Trust in order to protect the interests of the state and the rights of individuals and entities that use the products and services of the Trust;
      v) An outline of transition actions necessary for establishing the Trust; and
      vi) A draft of statutory and constitutional changes that may be necessary to establish the Trust.

EXISTING LAW:

1) Requires the Treasurer to receive and keep in the vaults of the Treasury or to deposit in banks or credit unions all moneys belonging to the state.

2) Requires the Controller to account for all expenditures as scheduled in the Budget Act including providing a monthly comparison between actual and estimated revenues.

3) Establishes various financing programs relating to housing, small business, infrastructure and schools. These programs are administered through multiple agencies under differing goals, processes and reporting requirements.

FISCAL EFFECT: Unknown

COMMENTS:

1) Purpose: According to the author, "California's economy has struggled to recover since the financial crisis of 2007. Finding ways to provide stability to our financial sector, reinvigorate our communities, and put people back to work will be a demanding process. Establishing the California Investment Trust is an important step in this process of rebuilding California's economy and addressing our current financial and community development challenges.

   The creation of the Task Force will look at ways in which California can create an Investment Trust to address the financial needs of the state in the long-run. This initiative has the great potential of increasing options for economic development which can include: low-interest credit for business retention and expansion, serving as a secondary market for mortgages and as a significant investor in municipal bonds, redevelopment finance and small business finance."

2) State Revenue Framework: AB 750 proposes to convene a Task Force to assess the viability of establishing a state bank that receives deposits of state moneys for the purpose of, among other things, spurring greater private economic activity and to reduce the cost of managing the state's funds. As a framework for considering this proposal, background information on the state's current structure for managing and investing the state funds is provided below and in the following comment.

   State government receives moneys from a variety of sources, including taxes, fees, revenue from the sale of bonds, and funds from the federal government. Responsible for managing these revenues are three primary government entities: the Treasurer, the Controller and the Director of the Department of Finance.

   The Treasurer serves as California's lead asset manager, banker and financier. Among other duties, the Treasurer's Office administers a number of bond finance authorities for specific community development activities, including funding for the development of housing, hospitals and alternative transportation vehicles. The Treasurer is also responsible for the custody of all money and securities belonging to, or held in trust by, the state; investment of temporarily idle state money, such as those in the Pooled Money Investment Account (PMIA); the sale of bonds and notes; and serves as the paying agent for all general obligation bonds and certain revenue bonds. Moneys available to the state may be held within the state treasury or in external accounts of financial institutions.

   Some programs, with the approval of the Department of Finance, may also hold state moneys in external financial institutions. Examples of state programs with external accounts include, but are not limited to, the California Infrastructure and Economic Development Bank, the Small Business Loan and Guarantee Program, and the California Capital Access Program.

   As the Department of Finance is the primary entity responsible for the preparation and oversight of the state budget, it is responsible for setting standards and practices for state agencies to follow in implementing their approved budgets. While the budget is an expenditure plan, actual revenues are needed to cover debts and other obligations. It is the role of the State Controller to closely monitor the amount of revenues available from all sources to meet California's financial obligations. On a monthly basis, the Controller issues a report with the state's actual cash balance. To the extent that there are insufficient funds to pay state expenses from the General Fund (GF), the Controller's Office may contact the

Treasurer to issue short-term debt (sometimes called revenue anticipation notes [RANs]) and/or assist in the internal borrowing of revenues against state Special Funds.

In the Controller's March 2011 "Statement of General Fund Cash Receipts and Disbursements," GF revenues were reported to be down by $370 million (-5.8%) from that projected in the budget. The state's outstanding loan balance for the period was $19 billion including $9 billion in internal borrowing from Special Funds and other accounts and $10 billion of external borrowing through RANs.

3) Examples of current activities with state revenues: Moneys that are not needed immediately for state expenditures are sometimes invested by the state. The PMIA is an example of when the Treasurer invests moneys that are not immediately required to pay state obligations. The PMIA has three primary sources of funds: the GF; special funds held by state agencies, which are managed through the Surplus Money Investment Fund (SMIF); and moneys deposited by cities, counties and other entities into the Local Agency Investment Fund (LAIF).

The PMIA is administered by a three-member Pooled Money Investment Board comprised of the Treasurer, the Controller and the Director of the Department of Finance. Participation in the PMIA provides local governments and the state with a safe investment alternative to simply holding moneys in no or low-interest bearing accounts and/or investing the moneys themselves.

PMIA investment policy sets as its primary investment objectives: safety, liquidity and yield. Existing law limits PMIA investments to U.S. government securities, securities of federally-sponsored agencies, domestic corporate bonds, interest-bearing time deposits in California banks, savings and loan associations and credit unions, prime-rated commercial paper, repurchase and reverse repurchase agreements, security loans, banker's acceptances, negotiable certificates of deposit and loans to various bond funds. In total, investment transactions with the State Treasurer's Office in the 2009-10 fiscal year included over 120 different financial institutions, including large federally chartered banks and small community development banks.

Although amounts varied greatly over the year, the PMIA's average daily fund level was $67.7 billion in earnings and $423.8 million in interest in fiscal year 2009-10. Approximately $156 million of this amount was interest credited to local governments who averaged $23.74 billion in deposits. The chart below provides additional details about the annual earnings of the PMIA.

Total Earnings of the PMIA for 2009-10		
1	General Fund	$41,527,666
2	Fish and Game Preservation Fund	$638,761
3	Surplus Money Investment Fund (SMIF)	$223,793,195
4	Local Agency Investment Fund (LAIF)	$156,372,921
5	Public Employee's Retirement Fund	$1,045,167
6	State Teacher's Retirement Fund	$425,172
	Total	**$423,803,882**
Source: Office of the State Treasurer, PMIA Annual Report 2009-10		

The earnings illustrated above consisted of $349 million from security investments at an average 0.69% yield, $9.4 million from time deposits at an average 0.20% yield, and $65 million from GF loans at an average 0.68% yield. The overall return on investment was 0.65%.

In general, the SMIF is comprised of "excess cash" from Special Funds that generally do not have their own investment authority. During the 2009-10 fiscal year, there were over one thousand special funds and accounts participating in the SMIF. Their combined deposits totaled $37,410,565,000 in 2009-10 fiscal year. The chart below lists the largest SMIF participants for the report period.

Large Contributors to Surplus Money Investment Fund (as of June 30, 2010)		
1	Department of Water Resources Electric Power Fund	$3,064,942,000
2	Highway Safety, Traffic Reduction Fund 2006	$2,556,397,000
3	Mental Health Services Fund	$2,440,938,000
4	Public Buildings Construction Fund	$1,866,221,000
5	California Housing Finance Fund	$1,686,471,000
6	Unemployment Compensation Disability Fund	$1,685,908,000
7	Safe Drinking Water Fund (2006)	$1,474,117,000
8	Disaster & Flood Bond Fund	$1,243,977,000
9	Housing/Emergency Shelter Fund	$1,162,851,000
10	Public Employees' Retirement Fund	$1,135,298,000
11	2006 State School Facilities Fund	$1,026,893,000
Source: Office of the State Treasurer		

While in good economic times excess GF related cash is invested through the PMIA, the PMIA can also serve as a vehicle for leveraging additional revenues to pay state GF obligations. According to the Treasurer's Office, approximately $6 billion of the state's portion of moneys in the PMIA have been borrowed against to meet current GF obligations, costing the state $65 million in interest in fiscal year 2009-10.

As the example of the PMIA illustrates, the state holds moneys in external accounts and that, even in difficult economic times, has a base amount of cash which, with prudent and proper management, is available for investment without endangering the state's financial status. Under the PMIA model, investment earnings are returned to the GF, special funds and local governments. AB 750 proposes that the Task Force consider whether a state bank model might provide even greater benefit or value to the state and local governments than current activities.

4) State bank models: In response to the financial crisis of 2007 and the resulting recession, a number of states have begun to consider whether it makes financial and policy sense to establish their own state banks. Modeled after the nearly 100-year old Bank of North Dakota (BND), legislators from states such as Washington, Oregon, Hawaii, Maine and Maryland have introduced bills to either establish state banks or study the establishment of a state bank.

   Common themes among the reasons stated for the establishment of the banks include the need to support economic development, provide stability to the local financial sectors, and to generate additional revenues for the state GF. Particularly attractive about the state bank model is its potential to help fill key access to capital gaps for entities such as small business start-ups and microenterprises. The two central challenges in establishing a state bank are the source of its initial capitalization and the role of the state bank within the context of other public and private financial institutions.

Below is a chart which illustrates the range of models being proposed in other state legislatures in 2011.

Comparison of State Bank Models in 2011 Legislation				
	Hawaii	Maine	Oregon	Washington
Bank Board or Executive Committee	Director of Finance (chair), 10 Governor appointees	5 Governor appointees	Governor (chair), Treasurer, Commissioner of the Bureau of Labor and Industries	Governor, Lt. Governor and Treasurer
Source of Deposits	All State Moneys plus Private Deposits	State Funds	All Public Funds and Any Source	Any Source, but all State Funds by June 30, 2015
Loan Types	Based on Adopted Rules	Loans to Banks and participation loans	Loans to Banks and Participation Loans	Loans in the Public Interest and subject to commission rules
Profits Returned to State	Not Stated	Determined by the Board	Determined by the Board with advice from Advisory Board	Determined by the Commission
Audit	State Commissioner of Financial Institutions	Quarterly examination by State Bureau of Financial Institutions and audit every 2 years	Quarterly audit by State Department of Consumer and Business Services and Secretary of State Audit every 2 years	Quarterly Report and Annual Report to State Commission
Backed by Full Faith and Credit of the State	Yes	Not Stated	Yes	Yes
Compiled from information provided on website of the Center for State Innovation 4/19/11				

Sufficient initial capitalization is central to the successful establishment of a state bank. In the case of the BND, it was funded with the proceeds of a $2 million bond. The Center for State Innovation (CSI) uses a $100 bond initial capitalization model and calculates bond repayments as part of the ongoing expenses of the bank. Based on CSI's capitalization model, CSI estimates that states can still expand the volume of economic and community development lending while meeting all debt obligations.

In addition to a bank's initial capitalization, state bank legislation also addresses the financial backing of overall bank activities, as well as individual financial products. Of the states reflected in the chart above, each utilizes the full faith and credit of the state. It should be noted however, that several California programs offer financial assistance through independently capitalized funds, which do not use the full faith and credit of the state including the Small Business Guarantee Program and the California Capital Access Program.

AB 750 proposes that a Task force examine one or more state bank models, report to the Legislature on its findings, and make a recommendation as to the viability of the establishment of the Trust.

5) Related legislation: The Governor has indicated that he is interested in streamlining and making state government more efficient including the potential for the reorganization of one or more state agencies and programs. AB 750 proposes to establish a Task Force, which would examine the viability of a state bank which could serve a variety of state and local financial needs.

The Assembly Committee on Jobs, Economic Development and the Economy is also reviewing legislation related to the California Infrastructure and Economic Development Bank. Descriptions of the bills are listed below.

a) AB 696 (Hueso) California Infrastructure and Economic Development Bank: This bill requires projects selected for funding under the Infrastructure State Revolving Fund Program to only be funded, if the project meets specified land use and economic development criteria. Status: Scheduled to be heard in the Assembly Committee on Jobs, Economic Development and the Economy on May 3, 2011.

b) AB 700 (Blumenfield) California Infrastructure and Economic Development Bank: This bill establishes an independently administered California Infrastructure and Economic Development Bank and removes the Secretary of the Business, Transportation and Housing Agency as chairperson. Status: Scheduled to be heard in the Assembly Committee on Jobs, Economic Development and the Economy on May 3, 2011.

c) AB 1094 (John A. Pérez) California Infrastructure and Economic Development Bank: This bill expands the membership of the board of directors of the Infrastructure Bank from five to seven members. Status: Scheduled to be heard in the Assembly Committee on Jobs, Economic Development and the Economy on May 3, 2011.

d) AB 893 (V. Manuel Pérez) California Infrastructure and Economic Development Bank: This bill modernizes the operations of the Infrastructure Bank, such as the inclusion of the economic development community on the Board, mandating outreach to communities, and adding new reporting requirements about the number of jobs created and retained, and the industries served. Status: Scheduled to be heard in the Assembly Committee on Jobs, Economic Development and the Economy on May 3, 2011.

REGISTERED SUPPORT / OPPOSITION:

Support

None on file

Opposition

None on file

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