

Date of Hearing: April 25, 2010

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Mike Eng, Chair
AB 1408 (B.& F. Committee) – As Introduced: March 9, 2011

SUBJECT: General obligation bonds

SUMMARY: Makes technical change to the State General Obligation Bond Law, to allow the minimum denomination of bonds that can be sold to \$25 or multiples of that sum.

EXISTING LAW

The State General Obligation Bond Law requires that bonds must be sold in minimum denominations of \$1000. (Government code, Section 16731).

FISCAL EFFECT: Unknown

COMMENTS:

This technical change to the law, sponsored by the State Treasurer

Section 16731(a) of The General Obligation Bond Law (GOBL) requires that General Obligation (GO) bonds be sold in minimum denominations of one thousand dollars (\$1,000) or multiples of that sum. In the past, this requirement worked well for the issuance of bonds since traditional fixed-rate bonds were generally sold in \$5,000 increments. However, due to the evolving nature of the bond market and the magnitude of authorized but unissued bonds remaining to be sold, flexibility is needed in determining the minimum denominations of bonds in order to achieve the best structure and rates possible for future bond sales. For example, one product that could potentially open up a largely untapped investor base requires that bonds be sold in minimum denominations of twenty-five dollars (\$25) or multiples thereof.

The California Alliance for Consumer Protection opposes this technical bill on several grounds including:

- 1) *Source: There is no identified funding source for this program. According to the Treasurer's office, there are around 100 outstanding, voter approved bonds on the books that have been approved since the early 60's that are still open for use by the state. As such, we need to ask, what funding source will the bonds come from? A follow up question is this: if it comes from a voter approved source or 'pot', will that source or fund benefit or be reimbursed? (In other words, if the money comes from voter approved educational bonds, shouldn't voter approved educational projects benefit and not the general fund?).*
- 2) *Policy: There is no overall direct marketing policy with respect to the program's implementation, oversight, operations and design. For example, how and where will consumers be able to purchase or redeem these items, and from whom? (Will consumers have to go to investment counselors or brokers or can consumers walk in and purchase or sell them at their neighborhood financial institution?).*

- 3) *Profitability: This measure begs the question, how much will it cost to make these products available to the public and how much will it cost small investors and consumers to purchase them? This is important because it will not only dictate costs for the state, but costs for the target market – the small investor. For example, if it costs \$10 to buy a \$25 bond and then \$10 to sell it, is that a benefit for the consumer or the State of California?*
- 4) *Costs to the state: I understand that this is a policy committee, and as such, the issue(s) I am going to raise here will be better addressed by either the Rev. and Tax Committee or the Budget Committee, but it should be placed on the table for review: Has anyone taken into consideration the overall costs to the state, not just in terms of running the project, but in terms of the “tax deductions” that consumers will be taking? For example, if it costs \$10 to buy the bond, and then \$10 to sell the bond, that is a combined \$20. If the bond pays a modest interest of say 5% over a 5 year period, will the state or consumer actually be making any money off the project? This question is based on long held concept that investors are allowed under tax law to deduct expenses related to the purchase and sale of investment items, and as such, those \$10 fees become tax deductions, especially when a profit is made. When you add in promotional, operation and unforeseen costs, we are begging this question: are we really making money or just transferring it from one pocket to another?*

In response to this opposition committee staff offers the following:

- 1) This bill does not establish a new program. It is a technical change to the state's General Obligation Bond law.
- 2) Since this bill does not create a new program, marketing outreach is not necessary.
- 3) This technical change will not cost the state or investors additional money. This is a technical change to give the Treasurer flexibility.
- 4) Finally, this bill does not establish a new program nor jeopardize the state's bond program. It is a technical change to an arbitrary bond denomination cap. This is designed to provide flexibility to Treasurer. Additionally, committee staff rejects the idea that the issues outlined in opponents #4 would be "better addressed" by other committees such as Rev & Tax or Budget Committee. Clearly, banking and finance staff have the necessary expertise to determine that this is a technical bill that does not establish a new program, nor does it impact or lead to any of the consequences raised by the opposition.

Amendments.

Committee staff suggests the following amendment to the Government code that also contains a reference to the minimum denomination of bonds.

16731.5. (a) Notwithstanding any other provision of this chapter, the committee may provide for the issuance of all or part of the bonds authorized to be issued as zero coupon or capital appreciation bonds. The committee shall adopt a resolution finding that issuance of these bonds is necessary and desirable, directing the Treasurer to arrange for preparation of the requisite

number of suitable bonds, and specifying other provisions relating to the bonds including the following:

(1) The date, number, denominations, and aggregate par value of the bonds payable at maturity. The aggregate par value may be represented by bond certificates in denominations as the committee deems appropriate, but not less than ~~one thousand dollars (\$1,000)~~ ***twenty-five dollars (\$25)***.

REGISTERED SUPPORT / OPPOSITION:

Support

California State Treasurer

Opposition

California Alliance for Consumer Protection (CACP)
www.TheCaliforniaIndex.org

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