

Senate Fiscal Agency
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SFA**BILL ANALYSIS**

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Senate Bill 1397 (as passed by the Senate)
Sponsor: Senator Joanne G. Emmons
Committee: Finance

Date Completed: 11-6-02

RATIONALE

Part 195 of the Natural Resources and Environmental Protection Act provides for the issuance of environmental protection bonds authorized under Part 193 of the Act. These are general obligation bonds approved by the voters in 1988 to finance environmental protection programs and to clean up contamination. The State Administrative Board is the administrator of the bonds. Part 195 authorizes the Board to issue the bonds in series, determine the interest rate or rates, issue refunding bonds, authorize insurance contracts and lines of credit, and generally administer the bonds to ensure their marketability, insurability, and tax-exempt status. It has been pointed out that Part 195 does not give the Board specific authority to enter into interest rate swaps, hedges, or similar agreements with regard to the environmental protection bonds. Since swap or hedge agreements have become common in bonding transactions, it has been suggested that the Board be allowed to use them for the environmental protection bonds. Further, it has been suggested that Part 195 should specify that the bonds would be subject to the Agency Financing Reporting Act.

CONTENT

The bill would amend Part 195 of the Natural Resources and Environmental Protection Act to do the following:

- Allow the State Administrative Board, "[f]or the purpose of more effectively managing its debt service", to enter into an interest rate exchange or swap, hedge, or similar agreement with respect to its bonds or notes, on the terms and payable from the sources and with the security, if any, as determined by a resolution of the Board.

- Provide that the issuance of bonds under Part 193 would be subject to the Agency Financing Reporting Act.
- Specify that the bonds would not be subject to the Revised Municipal Finance Act.
- Eliminate requirements that the bonds be approved by the Department of Treasury before their issuance.

(Public Act 470 of 2002 created the Agency Financing Reporting Act, which requires State agencies, and municipalities issuing debt exempt from the Revised Municipal Finance Act, to file a statement of intent with the Department of Treasury before issuing a security, and to report certain information to the Department after issuing a security. Public Act 34 of 2001 created the Revised Municipal Finance Act to regulate borrowing by municipalities and their issuance of securities, and repealed the Municipal Finance Act.)

MCL 324.19503

BACKGROUND

According to the "Yahoo! Financial Glossary", the term "interest rate swap" means a binding agreement between counterparties to exchange periodic interest payments on some predetermined dollar principal, which is called the notional principal amount.

This source also defines "hedge" as a transaction that reduces the risk of an investment. "Hedging" is defined as a strategy designed to reduce investment risk using call options, put options, short-selling, or futures contracts, with the purpose of reducing the volatility of a portfolio by reducing the risk of loss.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Of the numerous statutes that allow bonding and prescribe requirements for the administration of bonds, many permit the bonding authority to enter into interest rate swaps, hedges, or other similar agreements designed to reduce risks or produce financial benefits. In fact, Part 196 of the Natural Resources and Environmental Protection Act contains a provision nearly identical to the one proposed in the bill; the provision allows the State Administrative Board to enter into swaps and hedges with respect to the Clean Michigan Initiative bonds authorized under Part 196. Other examples include the State Housing Development Authority (MCL 125.1422aa) and the Michigan Strategic Fund Board (MCL 125.2023(15)), which are allowed to use swaps and hedges. In addition, the Revised Municipal Finance Act authorizes municipalities to enter into an interest rate exchange or swap, hedge, or similar agreement (MCL 141.2317). The bill also would authorize the State Administrative Board to use these tools for the environmental protection bonds.

Legislative Analyst: George Towne

FISCAL IMPACT

The bill would have no significant fiscal impact on the State and no fiscal impact on local government.

Fiscal Analyst: David Zin

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.