HB 294

Department of Legislative Services

Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

House Bill 294 (Delegate Heller, *et al.*)
(Joint Committee on the Management of Public Funds)
Appropriations Budget and Taxation

Bonds - Small Denominations

This bill increases the maximum amount of a small denomination bond from $1,000 to $5,000.

Fiscal Summary

State Effect: The bill's provisions would not directly affect governmental operations or finances.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: "Small denomination bonds" mean bonds in denominations of $1,000 or less. The Board of Public Works (BPW) may designate that all or a portion of State bonds be issued as small denomination bonds in a resolution regarding the terms of any State bond issue. Small denomination bonds may be issued in any form authorized by law.

BPW may sell small denomination bonds at a negotiated sale (where an underwriter bids for the right to manage the bond issue) if BPW determines that a negotiated sale will result in a more efficient or economical bond sale or provide greater access to investors who are State residents.

Background: This bill was proposed by the State Treasurer during a meeting with the Joint Committee on the Management of Public Funds on October 25, 2005. The Treasurer asked the committee to sponsor the bill so that BPW could consider resuming retail sales of general obligation bonds to the general public.

BPW currently has authority to issue general obligation bonds in denominations of $1,000 or less for sale to the public, but administration of those sales would be extremely burdensome. Until the 1980s, Maryland authorized "Mini-bonds" in denominations of $500, which were sold directly to Maryland residents. Because contracting with an underwriter to manage the sales, registration, and other logistics was prohibitively expensive for such a small bond issue, the Treasurer's Office acted as bond registrar and seller. Although the small bond sales were popular with Maryland residents, the administration became too difficult and the bond sales were discontinued.

Increasing the maximum of a small denomination bond to $5,000 would make administration of their sale economically feasible to contract out to an underwriter, who would be responsible for all management aspects. Generally, $5,000 is the industry standard so underwriters routinely handle the sale of bonds with denominations of $5,000 or higher.

In the event BPW determines that it would be appropriate to resume retail bond sales, this change would allow BPW, under its existing authority, to offer a portion of a bond sale to be sold at the retail level, through the services of an underwriter, directly to Maryland residents. After a prescribed "retail period," the balance of Maryland bonds could be sold in a public competitive sale as is now done.

A similar program has been successfully implemented in Delaware, another state with a "AAA" bond rating. A retail bond sale program would probably not result in any large interest savings for the State, but Maryland residents would be able to directly purchase general obligation bonds.

While wealthy investors can try to acquire Maryland general obligation bonds through the purchase of mutual fund shares, Maryland bonds are only rarely available. Maryland general obligation bonds are in extremely high demand because of their AAA bond rating. When general obligation bonds are sold (usually in February and July annually) large institutions such as Citigroup or Merrill Lynch purchase the entire series and remarket them to institutional buyers, who absorb all of Maryland's debt offerings.

Additional Information

Prior Introductions: None.

Cross File: SB 264 (Senator Lawlah, *et al.*) (Joint Committee on the Management of Public Funds) – Budget and Taxation.

Information Source(s): Department of Legislative Services

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Analysis by: Karen D. Morgan

Direct Inquiries to:
(410) 946-5510
(301) 970-5510