Department of Legislative Services

Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 809 (Delegate Heller, *et al.*) (Chair, Joint Committee on the Management of Public Funds)

Appropriations Budget and Taxation

State Debt - Annuity Bond Fund - Payment of Fiscal Agents

This bill authorizes the Annuity Bond Fund be used to pay ongoing costs of fiscal agents associated with variable interest rate bonds and interest rate exchange agreements.

The bill takes effect June 1, 2009.

Fiscal Summary

State Effect: The change is procedural in nature and does not directly affect State expenditures for debt service.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: The Comptroller credits money appropriated in the State budget to the Annuity Bond Fund to meet debt service requirements on State bonds. This money can be used to pay the principal and interest on debt. State law does not authorize the ongoing servicing costs of variable-rate debt to be paid from the Annuity Bond Fund.

Chapter 235 of 2003 authorized the State Treasurer to issue variable-rate bonds up to an amount equal to 15% of the State's outstanding general obligation bonds and to enter into interest rate exchange agreements or contracts. The State Treasurer may appoint any fiscal agents necessary to implement and administer such agreements or contracts. State law does not specify how the costs of fiscal agents may be paid.

Background: Historically, the State of Maryland has issued fixed-rate general obligation bonds for capital projects. The one-time costs associated with issuing fixed-rate bonds are paid directly from bond proceeds at the time of bond issuance. Fixed-rate bonds do not have ongoing servicing costs for fiscal agents.

To date, the State has not issued variable-rate bonds. Variable-rate demand bonds (VRDBs) do not have fixed interest rates throughout the life of the bond. Instead, VRDBs are constantly resold to lenders paying short-term interest rates. Unlike fixed-rate bonds, VRDBs do not have an underwriter. Instead, a remarketing agent manages bond sales. VRDBs also require a liquidity provider. Variable-rated debt is typically remarketed every week. If the remarketing agent cannot find another buyer for the debt, a liquidity provider is responsible for paying principal and interest for the bonds. VRDBs typically have a lower interest rate than fixed-rate bonds but also have ongoing servicing costs for fiscal agents such as remarketing agents and liquidity providers. These ongoing servicing costs cannot be paid from the bond proceeds in the same manner as one-time costs for fixed-rate bonds.

State Fiscal Effect: Under current law, if the State Treasurer issues variable-rate bonds, the ongoing cost of fiscal agents for those bonds is most likely paid with a series of special fund appropriations from bond proceeds. The Treasurer's Office estimates annual costs of $250,000 for each $100 million of variable debt issued. Authorizing payment from the Annuity Bond Fund for the cost of fiscal agents associated with variable interest rate bonds and interest rate exchange agreements has no overall effect on State expenditures for debt service, but may provide an operational benefit by not requiring separate appropriations for these expenses. The bill specifies that the ongoing servicing costs of variable-rate bonds be paid in the same manner as principal and interest.

Additional Information

Prior Introductions: None.

Cross File: SB 517 (Senator Jones, *et al.*) (Chair, Joint Committee on the Management of Public Funds) - Budget and Taxation.

Information Source(s): Department of Legislative Services

Fiscal Note History: First Reader - February 24, 2009 ncs/rhh

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Analysis by: Erik P. Timme

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