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Testimony in Support of AB 85

Doug Walther, Manager
Office of Business Finance and Planning
Department of Business and Industry

Good morning. My name is Doug Walther, and I am the Manager of the Office of Business Finance and Planning in the Director's Office of the Department of Business and Industry. Before explaining the provisions of AB 85 I would like to briefly explain how my office assists in the economic development of our state through the issuance of bonds for industrial development.

Industrial Development Bonds

Industrial development bonds, or IDBs, are essentially low interest loans to finance small manufacturing development, solid waste disposal projects and the activities of certain non-profit companies. Provisions of the federal tax code permit government entities such as my office to issue bonds, the interest on which is exempt from federal income tax. Investors are willing to accept a lower rate of interest on a tax-free IDB, and borrowers usually pay around 2 percent less than a comparable commercial loan. The program provides a strong incentive for manufacturers to relocate to or expand their operations in our state and for the development of other worthwhile projects.

Over the past twenty years my office has provided the financing for many manufacturers to relocate to or expand their facilities in Nevada, resulting in the creation of thousands of new jobs paying above-average wages. In addition, we have financed projects to reduce air pollution at mining operations, purchase cleaner burning trash collection vehicles and in the future hope to finance the purchase of needed medical equipment for qualified non-profit medical facilities. In 2000 my office issued $650 Million in private activity revenue bonds to finance the Las Vegas Monorail, a major transportation project that will reduce traffic congestion in Clark County, improve air quality and benefit our tourist economy, all without spending a single tax dollar. That project, I am happy to report, is on time and on budget, and expected to open to the public in the first quarter of 2004.

The Office of Business Finance and Planning is supported entirely by revenue generated by the program itself and requires no general fund appropriation. The federal tax code requires that IDBs be issued by a government entity and that other procedural steps be followed, such as conducting a public hearing on the project to be financed. Although issued by the State of Nevada, IDBs do not represent a legal or moral

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obligation of the state. Private investors provide the money for the loan and the beneficiary of the financing is obligated to make payments on the bonds. My office is considered a "conduit" for the financing, reviewing the application for compliance with the tax code, and making certain findings before issuing the bonds.

My office's role in an IDB financing is a critical, but limited one. We satisfy the code's technical requirements, market the program to qualified companies, assist applicants in understanding the requirements for IDB financing and help them assemble a team of professionals to complete the transaction. Just as important to the success of an IDB financing is the participation of bond professionals who ensure that the bonds can be successfully marketed to the private investment community. These professionals include banks and other financial institutions that guarantee the payments, market the bonds or purchase them directly for their own account. No IDB could be issued without their due diligence and review.

Mini Bond Program

Although IDBs are usually the least expensive means of financing eligible projects, they are more complex transactions that require more procedural steps, the involvement of more finance professionals and the payment of higher upfront fees and costs than conventional financing. Because of the time, effort and cost involved, in the past it has been uneconomical to finance projects smaller than $2.5 to $3 Million. In 1999, my office proposed and the legislature enacted what is now NRS 349.595 for equipment only financing. This statute was intended to simplify the process for financing smaller projects by allowing the State Board of Finance to adopt guidelines for the approval of such projects. Unfortunately, the statute did not clearly exempt such projects from other statutory requirements and the program has never been implemented.

Through our participation in the national Council of Development Finance Agencies (CDFA) we have learned that many states are making the benefits of IDB financing available to smaller projects by lowering costs and simplifying the approval process. Discussions with several financial institutions also indicate that much needed development capital could be made available if the approval process is simplified and the costs lowered. Over the past year my office has developed a Mini Bond Program to permit the financing of projects in the $500,000 to $3,000,000 range. We have lowered issuance costs by creating standardized transaction documents, placing caps on professional fees, and selling mini bonds only to sophisticated financial institutions, eliminating the need for, and cost of, underwriters and trustees. So far, Bank of America, Wells Fargo, GE Capital and Key Municipal Finance have agreed to participate in the program and purchase Mini Bonds for their own account. AB 85 is intended to further this process by exempting Mini Bonds from some of the more time consuming and costly steps of the approval process required for traditional IDBs.

AB 85 amends NRS 349.595 to clearly provide that bonds may be issued pursuant to its provisions as an alternative to issuing bonds pursuant to the provisions of NRS 349.380 and 349.390. In effect, the statute eliminates the requirement that the local government and Board of Finance approve the findings of the Director, although the Director, with two exceptions, is still required to make the findings required by those statutes. By authorizing the issuance of bonds based only on the Director's findings, we believe we will shorten the time, and associated expense, required to approve and issue Mini Bonds.

NRS 349.595 is limited to the issuance of bonds in amounts up to $3 Million in circumstances that the legislature has already recognized present less risk to the state. The bonds must be issued to institutional investors in denominations of at least $100,000 or receive an investment grade rating. These are the circumstances under which NRS 349.590(2) authorizes the waiving of the requirement that an applicant provide a five-year operating history.

In addition, since all participating investors qualify as "institutional buyers" under SEC rules, we believe it is unnecessary for the state to independently determine the feasibility of the project to be financed, as currently required by NRS 349.580(2)(c). Under current practice, our office charges each applicant at least $5,000 to obtain a professional consultant's review of the project and the obligor's financial situation. Since the participating financial institutions are underwriting the debt and performing their own due diligence regarding the feasibility of the project and the obligor's ability to meet debt service requirements, we wish to eliminate this expense for small, qualifying projects. The BDR therefore amends NRS 349.595 to eliminate the requirement that the Director make the finding set forth in NRS 349.580(2)(c). In effect, the Director may rely on a participating financial institution's decision to purchase the bonds as evidence of the feasibility of the project.

Finally, we wish to eliminate the requirement of NRS 349.580(2)(f) that a mini bond project be specifically related to economic development, tourism or the generation of electricity. Although most projects will further the state's general economic development goals, we do not want to disqualify a project whose public benefits are not so clearly tied to economic development, such as the purchase of needed medical equipment for a non-profit hospital.

I wish to emphasize that, although AB 85 removes the statutory requirement for the State Board of Finance to approve the Director's findings relating to IDBs, it will continue to play an important role in the approval of Mini Bonds. Under AB 85 and the existing provisions of NRS 349.595(2), the Board must establish guidelines for the issuance of Mini Bonds. My office intends to request the Board, consisting of the Governor, Treasurer, Controller and two public members, to retain its current practice of reviewing and approving *all* IDB transactions, including Mini Bonds. If further experience with the program reveals a need to modify those procedures, the Board will be able to do so without having to seek an amendment to the statute.

I also wish to emphasize that, although AB 85 will eliminate the statutory requirement that the local government in which the project will be located formally approve the Director's findings with regard to Mini Bonds, local governments will continue to play an important role in the process. Most projects involving construction or expansion require local government involvement in the permitting and zoning process. We also intend to solicit local government participation in the public hearing required by the tax code which always takes place in the jurisdiction where the project is located. State volume cap, or bonding authority, is required for all manufacturing projects. It is our practice to request the effected local government to commit a portion of its volume cap to such a project, which must be accomplished through the passage of a formal resolution. This will provide yet another means to consider the views of local government. Finally, a local government may express its views regarding a project either formally through the passage of a resolution or informally though staff communication with my office. We will not issue Mini Bonds to finance projects that face strong local opposition.

In summary, AB 85 will help open up a source of much needed, but previously unavailable, development capital, allow the financing of many worthwhile, but smaller projects that will create jobs and other benefits for our state, and will not significantly increase the risk to the State of Nevada. I would be happy to answer any questions you may have about the bill or the Mini Bond Program.

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