

Department of Legislative Services
Maryland General Assembly
2023 Session

FISCAL AND POLICY NOTE
Third Reader

House Bill 397
Appropriations

(Delegate Watson)

Budget and Taxation

State Investment Portfolio - Investment Thresholds - Alterations

This bill requires the State Treasurer to adopt regulations establishing a State investment policy that specifies thresholds for maximum investment in each asset class in which the State Treasurer is authorized to invest or reinvest unexpended or surplus money. The bill also repeals the maximum threshold of 10% of total investments for investments the State Treasurer makes in the commercial paper asset class. Prior to the effective date of the bill, the State Treasurer must notify in writing the chief executive and governing body of each local governmental unit required to have a local investment policy under § 17-205 of the Local Government Article. The State Treasurer must also provide the local government with an opportunity to review, revise, and report any changes in the local investment policies, as appropriate. **The bill takes effect June 1, 2023, and the State Treasurer must adopt regulations under the bill by December 1, 2023.**

Fiscal Summary

State Effect: General fund revenues may increase by an indeterminate amount beginning in FY 2024 to the extent higher investment returns are realized through increased investment in commercial paper under the bill, as discussed below. State expenditures are not affected.

Local Effect: Revenues for certain local government entities may be minimally affected, as discussed below. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law: The State Treasurer may invest or reinvest unexpended or surplus money in:

- an obligation for which the United States has pledged its faith and credit for the payment of the principal and interest;
- an obligation that a federal agency or a federal instrumentality has issued in accordance with an act of Congress;
- an obligation issued and unconditionally guaranteed by a supranational issuer;
- a repurchase agreement collateralized in an amount not less than 102% of the principal amount by an obligation of the United States, its agencies, or instrumentalities;
- bankers' acceptances guaranteed by a financial institution with a short-term debt rating in the highest letter and numerical rating by at least one nationally recognized statistical rating organization as designated by either the United States Securities and Exchange Commission or the State Treasurer;
- with respect to amounts treated by the Internal Revenue Service as bond sale proceeds only, bonds, notes, or other obligations of investment grade in the highest quality letter and numerical rating by at least one nationally recognized statistical rating organization as designated by the United States Securities and Exchange Commission issued by or on behalf of this or any other state or any agency, department, county, municipal or public corporation, special district, authority, or political subdivision thereof, or in any fund or trust that invests only in securities of the type described in this item;
- commercial paper that has received the highest letter and numerical rating by at least two nationally recognized statistical rating organizations as designated by the United States Securities and Exchange Commission provided that such commercial paper does not exceed 10% of the total investments made by the State Treasurer;
- money market mutual funds with certain restrictions; and
- any investment portfolio created under the Maryland Local Government Investment Pool.

The State Treasurer is required to report to the General Assembly annually by January 3 on investment activities. At a minimum, the report must contain the following information for general fund investments and all other investments:

- the inventory of investments with maturity dates and the book and market value as of June 30;
- the earned net income;

- the percentage share of each category of investment in the portfolio; and
- sales of investments prior to the maturity date.

The State Treasurer is required to make investments with care, skill, prudence, and diligence with due regard for minimizing risk while maximizing return. The State Treasurer must use competitive purchasing practices except when impractical. Investments must reasonably match the State's cash flow so that sufficient funds are available to pay obligations as they become due. The State Treasurer must also maintain a reasonable amount of cash on hand for unanticipated needs. Investments must be made accordance with a written investment policy, and they must be made so that securities and collateral may be priced on a market-to-market basis. The State Treasurer must also avoid the enhancement of his/her personal financial position and avoid enhancing the personal financial positions of employees who are responsible for managing investments with State funds.

The State Treasurer must attempt to use minority business enterprises for brokerage and investment management services for its investments to the greatest extent feasible.

Local Investment Policy

Local governments are required to establish and follow an investment policy for specified public funds that is consistent with guidelines established by the State Treasurer. For this requirement, local government includes Baltimore City, counties, municipalities, community colleges, the Washington Suburban Sanitary Commission, public corporations, and authorities of the State that issue debt. Investments by a board of education and a library board must comply with the respective county local investment policy. The public funds subject to the required policy do not include revenues held as part of a pension fund, other postemployment fund, or trust fund account. Borrowing of funds for the express purpose of investing those funds is prohibited.

The Maryland Code of Regulations (COMAR 25.03.03.03) requires that a local government investment policy meets or exceeds standards published by two nationally recognized financial organizations that are recognized by the State Treasurer: the Municipal Treasurer's Association; and the Government Finance Officers Association. COMAR 25.03.03.04 requires that local government units invest in only those types of securities authorized by the State Finance and Procurement Article § 6-222(a), thus aligning permissible investments of local governments with limits that must be followed by the State Treasurer.

State Revenues: The bill provides the State Treasurer with more flexibility to manage its investment portfolio and repeals the maximum threshold of 10% of total investments for investments the State Treasurer makes in the commercial paper asset class. The

State Treasurer notes that a recent survey of AAA-rated states found that many of these states do not limit the maximum investment in commercial paper. For states that do establish a threshold on investment in commercial paper, these thresholds can be as high as 50% of total investments.

The State Treasurer advises that approximately \$2 billion (9.3%) of its estimated current \$21.8 billion total investment portfolio is in the commercial paper asset class, and the percentage invested in commercial paper would likely increase under the bill. The bill would bring the State more in line with other top-rated states, which could potentially yield a higher rate of return for the State's investments. However, the amount of additional revenue cannot be reliably estimated as it would depend on how each investment performs relative to other investment classes.

Local Revenues: Local governments are required to establish and follow an investment policy for specified public funds that is consistent with guidelines established by the State Treasurer. For those local governments that invest in commercial paper, the elimination of the maximum threshold in allowable commercial paper investment will provide greater flexibility in investing in those types of assets and could potentially yield a higher rate of return for local investments; however, the amount of additional revenue cannot be reliably estimated, as discussed above.

Additional Information

Prior Introductions: Similar legislation has not been introduced within the last three years.

Designated Cross File: SB 153 (Senator Augustine)(Chair, Joint Committee on the Management of Public Funds) - Budget and Taxation.

Information Source(s): State Treasurer's Office; Department of Legislative Services

Fiscal Note History: First Reader - January 27, 2023
rh/hlb Third Reader - March 7, 2023

Analysis by: Trevor S. Owen

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