TOM SGOUROS · www.sgouros.com

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Joint Committee on Community Development and Small Businesses
Honorable Edward Coppinger, House chair
Massachusetts State House
24 Beacon St,
Boston, MA 02133

RE: Testimony in Favor of HD 3543

Honorable Committee:

During 2015 and 2016, I served as Senior Policy Advisor to Rhode Island General Treasurer Seth Magaziner. One of the primary projects I took on was to help design and write legislation for the new Rhode Island Infrastructure Bank (RIIB). The legislation passed in 2015, and it has already become a vital institution and is poised to grow and do things we did not imagine. Its benefit to the state, in terms of roads (re)built and clean energy projects underway, is already substantial and in the future it will only grow.

With your indulgence, I would like to share a couple of lessons learned along the way. To be clear, but these are my observations, and not the Treasurer's.

To create RIIB, we built on a small finance agency focused on water projects, so essentially the task was only to add some more flexible lending programs to an already-existing, well-run, agency. The old Clean Water Finance Agency was well used to doing bond finance, and bond finance was envisioned for the new programs. There was substantial demand from the state's municipalities for the new programs, for roads and bridges, and for energy finance. In fact, the demand was far greater than the capacity from the beginning.

Sole reliance on the bond market was problematic for a few reasons. The first is that trying to corral a dozen municipal projects into a bond issue is a long and tedious process. More than a few of the projects could have been completed months, possibly years, sooner but for financing delays caused by wrangling all the other municipalities into the same pool. Second, because we sought a rating for the bond, not the lending program or the institution, we were unable to concentrate the lending in the communities that need it the most. The logic of sharing risk as expressed in bond documents meant that our bonds would involve lending in rich communities, as well as poor ones. This is not a bad thing in some respects—rich communities have legitimate need for attention from the state, too—but the aid we can get this way is out of proportion to the needs.

The bond market is also inflexible. Programs must be envisioned completely enough to be thoroughly described in bond documents. A thorough airing of public policies is always a good thing, but it is not unknown for conditions to change. Once a bond is sold, the terms are immutable, and this can deprive the institution of adapting to unforeseen market developments and municipal needs.

The other important issue is that the state has many more loanable resources available to it than precedent would seem to allow. For example, National Grid collects about $100 million annually from the systems benefits charge on consumer electric bills, to be used for clean energy and conservation projects, as in Massachusetts. At any one time, there are between $4 and $10 million in collected, but unspent, funds. National Grid's bank is reaping the benefit of the "float" on that account, not the ratepayers. Why not let the state use that? It could be a useful component of the liquidity of a more agile and powerful green infrastructure bank.

In a similar vein, the cash management operation at Treasury was contenting itself with investing in short-term CDs and notes at about 30–40 basis points of interest. Meanwhile RIIB was selling short-term bond-anticipation notes at 2–2.5%. Why, the RIIB CFO asked, can't we sell our notes to Treasury at 1%? Both of us would come out ahead. A quick analysis I completed showed there is easily enough cash on deposit or invested short like this around our state to safely double the capacity of the infrastructure bank, possibly more.

I'm pleased to report that the early success of the RIIB programs, and the appointment of a more ambitious board chair have led to several of these ideas being reconsidered as the institution seeks to expand its capacity and flexibility. But that very progress has also made it clear that opportunities were missed at the design stage that would have made RIIB more effective at helping our municipalities with their needs, and that's the important bottom line.

The lesson of our experience are that one should create an institution strong enough to be rated on its own. This would have allowed us to steer aid to the communities that need it the most, rather than always averaging their needs with those of more affluent communities. This means capitalizing it and providing it with access to liquidity reserves of some kind. One way to accomplish that is to give it the flexibility to supply some of the state's own cash management needs.

There are a couple of useful models to be found in other states that already incorporate some of these lessons. The state-owned bank in North Dakota is a good example of an institution with the flexibility and financial strength to do a tremendous amount of good on behalf of that state's economy. It manages the state's cash and thereby has the financial capacity to fulfill a lot of the state's borrowing needs, as well as the flexibility to create programs on the fly, such as providing emergency credit to rebuild ravaged communities after the disastrous floods of 2011 in Minot and Bismarck or 1997 in Grand Forks.

Closer to home, the state of Vermont developed an internal investment program in 2014 that allows the state's cash balance to be invested safely on the short term to provide loanable funds for affordable housing, green energy projects, and economic development. While somewhat short of being a bank, the program nevertheless demonstrates that such rearrangements of financial precedent are not that difficult, and can have a great benefit to the state while at the same time tightly controlling risk.

I have reviewed some of the legislation before this committee. HB1763 seems to me comparable to the RIIB enabling legislation we developed in 2015. I would strongly endorse this legislation, but only as a first step in growing a strong new lending institution to take on these important needs. In contrast, HB3543 seems already to have incorporated the lessons we learned in Rhode Island. Creating a green infrastructure bank for the state of Massachusetts that is powerful and secure—and able to use the state's own financial strength on behalf of its citizens—would have far-reaching benefits to the state.

Sincerely,

Tom Sgouros