

HOUSE BILL REPORT

SB 5142

As Passed House - Amended:

April 13, 1995

Title: An act relating to payment agreements.

Brief Description: Extending authority to enter into payment agreements.

Sponsors: Senators Quigley and Sellar.

Brief History:

Committee Activity:

Financial Institutions & Insurance: 3/20/95, 3/22/95 [DPA].

Floor Activity:

Amended.

Passed House: 4/13/95, 95-0.

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: Do pass as amended. Signed by 14 members: Representatives L. Thomas, Chairman; Beeksma, Vice Chairman; Smith, Vice Chairman; Wolfe, Ranking Minority Member; Grant, Assistant Ranking Minority Member; Benton; Campbell; Costa; Dellwo; Dyer; Huff; Kessler; Ogden and Pelesky.

Staff: Charlie Gavigan (786-7340).

Background: Much of the construction or acquisition of capital facilities by state and local governments is financed by long-term debt instruments including revenue bonds, general obligation bonds, lease-purchase agreements, notes and other contractual arrangements. All of these arrangements include obligations to make payments which include interest. The interest, which is generally at a fixed rate, is determined by the financial markets at the time the obligation is incurred.

Because market interest rates constantly fluctuate, the financial community has developed a mechanism for parties to swap their respective payment obligations when it is in their mutual interest. These are side contracts which do not alter the basic obligations. One party agrees to make the payments owed by the other party and vice versa for a fixed period of time. This may enable a party with a fixed-rate obligation to take advantage of lower interest rates available on a variable-rate obligation while

the swapping party obtains the advantage of reducing his or her exposure to the risk of rising interest rates.

In 1993, some governmental entities were authorized to enter into a payment agreement in connection with specific obligations for the purpose of managing or reducing exposure to fluctuations of interest rates.

These governmental entities include the State Finance Committee, the Washington Health Care Facilities Authority, the Washington Higher Education Facilities Authority, the Washington State Housing Finance Commission and any city, county, port district or public utility district which has or will have at the time of entering a payment agreement \$100 million in outstanding obligations or had at least \$100 million in gross revenue in the preceding calendar year.

Prior to entering a payment agreement, the governmental entity must, by ordinance or resolution, make a finding that the transaction will reduce the amount or duration of its exposure to interest rate changes, reduce the cost of borrowing, or increase the rate of return on investments made in connection with the obligation. The governmental entity must obtain a written certification from a qualified and disinterested financial advisor that its findings are reasonable.

A payment agreement may only be entered with a party that has a rating from at least two nationally recognized credit rating agencies that is within either (1) the two highest long-term investment grade rating categories, or (2) the three highest long-term investment grade rating categories if the obligation of the other party is collateralized by direct obligations of or obligations guaranteed by the United States of America.

The term and notional amount of the payment agreement may not exceed the term and principal amount of the obligation on which the agreement is based. If otherwise permissible, any rates or taxes tied to the underlying obligation may be adjusted to reflect the requirements of a payment agreement.

The authority to enter new payment agreements expires on June 30, 1995, except to replace an existing payment agreement if based upon the same underlying obligation.

Summary of Bill: The authority for certain government entities to enter into payment agreements to reduce interest on bonds and other contractual obligations is extended until June 30, 2000. The State Finance Committee is required to make annual reports to the Legislature.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date of Bill: The bill contains an emergency clause and takes effect on July 1, 1995.

Testimony For: This bill continues a program that safely gives the state and some local governments the ability to enter into agreements that can reduce interest payments on public obligations.

Testimony Against: None.

Testified: Senator Quigley, prime sponsor; and Tim Kerr, State Treasurers Office.