PIEC003

Economic Development Bonds

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PROPOSED CONSTITUTIONAL AMENDMENT NO. 2

(Referred to the People by the General Assembly)

POPULAR NAME: An amendment to allow the General Assembly to approve the issuance of general obligation bonds for any economic development project that plans to invest more than $500 million in capital expenditures and to hire more than 500 new employees.

BALLOT TITLE:

Proposing a constitutional amendment to allow the Arkansas General Assembly, meeting in regular or special session, to approve a general obligation bond or bonds, not to exceed five percent (5%) of state general revenues, for the purpose of providing infrastructure and other needs to attract economic development projects investing a minimum of five hundred million dollars ($500,000,000) and creating a minimum of five hundred (500) jobs.

BALLOT SUBTITLE:

Proposing a constitutional amendment to allow the Arkansas General Assembly to approve general obligation bonds for economic development projects.

Why is the issue on the ballot of a General Election?

By approving House Joint Resolution 1028, the state legislature has proposed amending the Arkansas Constitution to include Proposed Constitutional Amendment No. 2. All constitutional amendments require approval by a majority of voters in a statewide election.

What does this amendment do?

Proposed Constitutional Amendment No. 2 would allow the legislature to authorize the Arkansas Development Finance Authority to issue general obligation bonds to attract large economic development projects, also called super projects, under the following circumstances:

- The bonds are issued to finance a variety of infrastructure needs, such as land acquisition, site preparation, road improvements, rail spurs, water and waste service, employee training, environmental mitigation or training or research facilities.
- Bond issues cannot exceed 5 percent of the state's most recent year general revenues collected.
- The prospective company must be planning to invest at least $500 million in the project and plan to hire at least 500 new employees.
- Costs associated with the bonds must be paid using general or special revenues appropriated by the General Assembly.

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- Empowers the Arkansas Legislature to vote on bond issues for economic development infrastructure rather than requiring a vote of the people.

What is a general obligation bond?

In this context, a bond is a certificate of debt issued by the state. In return for purchasing the bond, the bond holder (investor) will receive interest payments as well as the original investment on a schedule predetermined at the time the bond is issued. In consumer terms, this could be considered similar to taking out a long-term loan to buy a house. A general obligation bond is legally backed by the full faith and credit of the issuing government, in this case, the State of Arkansas. This means that costs associated with the bonds (interest payments and principal repayment) will be paid using any revenue source available to the state.

Because of full faith and credit backing, general obligation bonds are considered low risk by investors. This allows states to sell bonds, or borrow money, at relatively low interest rates. The bonds are typically used to finance large capital projects, which are costly and difficult to pay at once. Typically, the benefits derived from the investment are expected to continue for the life of the bond issue or beyond. Examples of large capital projects include land purchases, the development or improvement of facilities, roads and highways, water or waste treatment or other infrastructure projects.

What does the constitution currently say about issuing state bonds?

Amendment 20 of the Arkansas Constitution says that the state may issue new bonds only if approved by a majority vote in a general or special election.

Arkansas Code (7-9-13) requires that the Secretary of State provide public notice of such measures 8 weeks prior to the election. Notice must be provided in 2 weekly issues of newspapers in each county.

Amendment 65 states that revenue bonds may be issued by the state without an election. A revenue bond is different from a general obligation bond.

- A revenue bond must be secured by revenues resulting from the project or improvement for which it is issued.
- A general obligation bond is secured by any revenue source available to the state.

How is the 5% cap applied?

The ballot measure does not specify. Section 1 (b) of the proposed amendment reads: "Bonds may be issued for an amount up to five percent (5%) of state general revenues collected during the most recent fiscal year." The amendment does not specify whether this is a rolling limit or an annual limit or whether it applies to gross or net general revenues.

What costs are associated with the issuance of these bonds?

It depends on the terms of the bond issue. The proposed amendment limits the bond issue amount to 5 percent of the state's general revenues. According to the Arkansas Department of Finance and Administration web site, fiscal year 2003 gross general revenues were just over $4 billion. Using this number as an example, a maximum issue of 5 percent would be approximately $202 million. To retire the bonds, the state would have to repay that total amount issued, plus the interest payments associated with it, over a specified period of time.

The following is an example of how a bond issue might be structured, for illustrative purposes only. It is not an estimate of actual costs.

Suppose the General Assembly voted to approve the issue of $100 million in general obligation bonds. If the bond issue consists of 20-year serial bonds with a 5 percent interest rate, annual principal payments would equal $5 million ($100 million ÷ 20 years). Interest payments would decrease over time as the debt is paid down. In the first year, the interest payment would be $5 million since the entire debt is outstanding ($100 million x 5%). Thus total debt payment (principal and interest) in the first year would equal $10 million. In the second year, the debt outstanding would be $95 million, resulting in an interest payment of $4.75 million ($95 million x 5%) and a total debt payment of $9.75 million. Payments would continue in this manner over the 20 years until the debt is retired.

So for this example, in return for receiving $100 million from the sale of general obligation bonds, the state would pay an average of $7.6 million per year to repay the principal and make the interest payments.

How would the costs of general obligation bonds issued under this amendment be paid?

The bonds will be paid for using general or special revenues appropriated by the General Assembly. General revenues primarily consist of income taxes (individual and corporate) and sales or use taxes. Special revenues consist of taxes or fees collected in accordance with Arkansas law to support specific state programs or agency costs.

What benefits are associated with super projects?

It is impossible to estimate specific benefits of this proposed amendment without knowing specific details about an economic development project. In general, goals of economic development include increasing the number of jobs, income and productivity. Additional revenues generated by a number of higher-paying jobs could make principal and interest payments on the bonds and provide a substantial increase in overall state tax collections. More jobs and higher personal income levels could also lessen the need for unemployment and welfare program expenditures by the state. Other indirect benefits could also occur.

How long will a company have to make the required investment and hire new employees?

The ballot measure does not specify. Section 1 (d) of the proposed amendment reads: "In order for the General Assembly to authorize the issuance of bonds bearing the full faith and credit of the State of Arkansas, the prospective employer must be planning an economic development project that will invest more than five hundred million dollars ($500,000,000) in capital expenditures and plan on hiring over five hundred (500) new employees." In deciding whether to issue bonds in support of a project, the Legislature will need to evaluate the prospective employer's investment plans and determine whether the plan is worthy of a commitment of state resources.

How will the legislature determine when and how to issue economic development bonds?

The proposed amendment does not specify a process for determining how and when the amendment would be used. If this proposed amendment passes, specific rules, regulations and safeguards will be developed to address these issues.

The following statements are what supporters and opponents of the constitutional amendment report in their literature and on their web sites. By presenting these statements the University of Arkansas does not endorse or in any way validate the statements.

What do supporters say?

Supporters believe that allowing the General Assembly to issue bonds will demonstrate to businesses and industries that Arkansas is capable of responding to their needs in a timely manner. They cite a study commissioned by the 2001 Arkansas Legislature to assess the state's competitiveness in attracting super projects. Supporters say that super projects will:

- Generate increased tax revenues, which can be used to improve education, health care and roads, while allowing the state to make the principal and interest payments associated with the bonds.
- Create additional secondary jobs as other plants and investments locate in Arkansas to support the super project.

What do opponents say?

At the time this fact was published, no organized opposition was identified. The following statements reflect sentiments voiced by individuals in forums where this proposed amendment has been discussed.

- There are only a few locations in Arkansas that are suitable for the types of projects that this amendment would support, based on the required investment and employment levels.
- In light of current commitments to increase funding for public education, Arkansas cannot afford to incur additional demands from already stretched state revenues.

When does the legislation take effect if passed?

The amendment, if passed, would become effective on January 1, 2005.

What does a "yes" vote mean?

The Arkansas Legislature will have the authority to approve the issuance of general obligation bonds to finance infrastructure improvements in support of large economic development projects under the restrictions specified in this proposed amendment and subsequent legislation.

What does a "no" vote mean?

The issuance of general obligation bonds by the state will continue to require approval of a majority of voters in a general or special election called for that purpose.

Where can I find more information?

The complete and official text of each ballot measure can be obtained through the Arkansas Secretary of State's office:

- Phone: 501-682-1010
- Web site: http://www.sos.arkansas.gov/elections_proposed_amendments.html

For other information, including major support and opposition groups, please visit our web site (http://piec.uaex.edu) or contact your county Cooperative Extension Service office.

Exercise your voting privilege.

We live in a democratic society where voting is both an obligation and a privilege of citizenship. Democracy works best when informed citizens exercise their voting privilege. Please vote November 2, 2004.

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