

2013 HOUSE INDUSTRY, BUSINESS AND LABOR

HB 1078

2013 HOUSE STANDING COMMITTEE MINUTES

House Industry, Business and Labor Committee
Peace Garden Room, State Capitol

HB 1078

January 9, 2013

Job 17043, starting at minute 6:53
(recording also contains HB 1052)

Conference Committee

Committee Clerk Signature

Explanation or reason for introduction of bill/resolution:

Relating to the investment of funds by the Bank of North Dakota

Minutes:

Attachment #1

(6:53) Hearing opened.

Chairman Keiser: Thank you for coming in a little earlier than you had thought you'd need to come in.

Bob Humann from the Bank of North Dakota: Provided Attachment 1 for reference. The New Venture Capital Program has been around since 2003. For the New Venture Capital Program, there is a ceiling of \$10 million right now which we want to increase to \$15 million. We started off in 2003 with a \$5 million allotment of money, which is basically the bank's deposit money which we're employing in investments, and we're employing in subordinated debt loans. The legislature in 2005 approved another \$5 million, so that brings us to the current \$10 million dollar allocation that we can spend with this program. There is currently about \$1.5 million left in program right now. With all the activity we have going on in the state, we feel we should have more availability in case things really pick up during the next biennium.

The program has been a good tool to be able to help start-up businesses. Businesses are starved for start-up capital. This is a venture capital system where they can come to get some dollars. We've turned the servicing of this fund over to the North Dakota Development Fund. It's a great tool for Dean Reese and the Development Fund to be able to leverage dollars out of the North Dakota Development Fund and then the New Venture Capital Program.

What we found when we started this program is that we were making investments in companies, they'd be successful, and then two years later the company would want us to participate in a PACE loan, for example. It seemed like we were investing in a company, we're an owner in the company, and then we're turning around and approving a loan for the same company. That did not sound right or feel right in banking. So we turned the servicing over to the Development Fund, but it is still the bank's money. That has worked out great, just as we wanted it to work. At the end of the day, they have more expertise in equity investments into companies.

Chairman Keiser: Questions? Where does the money come from? Is the money out of the profits of the Bank of North Dakota? Are we taking an equity position with these dollars in these companies, or is it a loan, or is it a grant?

Humann: It is not different that how we'd fund any loan at the bank. It is out of our liquidity sources, which is primarily deposits. We were so flush with state deposits due to all the oil and gas revenue coming to the bank. So it's our deposit money which we're employing, just like we would a loan. These dollars in the New Venture Capital Program are a combination of loans and a combination of investments. When it comes to loans, we are taking a subordinated debt position behind another lender that is willing to do something with the company and wants to have the primary assets involved. We are helping them to grow. This is really a subordinated debt position. We take an equity position in there, too. It goes on our books at the bank as an investment, just like if we were buying mortgage-backed securities or US treasuries.

Representative Boschee: When it's a loan, is there interest accrued that the bank receives? What are the financial benefits for the bank?

Humann: There are interest rates on the loans, ranging from 4 to 6 percent. We try to keep it below market rate. Keep in mind that if you went to a true venture capital firm, they would be charging anywhere from 8 to 16 percent for venture capital money. So for us to come in as a state and do 4 to 6 percent, it is more attractive than any other source they could get for someone to invest in their company. If they went to Wall Street brokers and they tried to raise money, it would be closer to the high teens.

Representative Sukut: When you look at the bad debt ratio for this program, and compare it to the normal bad debt ratio, how those compare?

Humann: We actually have additional losses here, losses that would exceed what we do in our bank portfolio. A lot of these are start-up companies, and we are kind of guessing whether or not they will work. This is no different than most startups. It comes down to the management, whether or not they have a proper amount of equity. It comes down to the type of business they're trying to get into and whether they have the right business model for the right time. Our losses here do exceed our normal loan portfolio, but keep in mind that there are smaller loans and investments. They do not exceed \$300,000 to \$500,000. Normally, our cap is \$300,000 for the loans and investments within this program per borrower. What Dean Reese and the North Dakota Development Fund are excellent at doing is that they will stage the loans or investments such that if the borrower comes up with \$150,000, we'll match that amount through the New Venture Capital Program. That shows that the owner has a stake in the game and is not just playing with the state's money and not keeping their eye on the ball.

Representative Becker: So you do worse with this program than with normal lending. Do you have actual numbers?

Humann: Yes, I do have actual numbers. I do not have a breakdown between the loan losses and the investment losses, but I can give you a total. Since 2003, of the \$8.5 million that we have ended up funding so far, we have lost \$1.1 million. Right now, we have a \$3 billion loan portfolio, and a ballpark figure of our charge offs will be less than \$3 million.

Chairman Keiser: On your balance sheet, are you just transferring dollars?

Humann: This just gives us the authority to do another \$5 million. But you're right. When we do a loan, it shows up as a loan on our balance sheet. When we do an investment, it shows up as an investment on our balance sheet. The reason is that we do administer a lot of different funds that are not part of the bank's balance sheet, such as the Community Water Facility Loan Fund. We have other funds we administer. However, this is not a separate fund; it's a program. These are actually the bank's assets.

Chairman Keiser: Do I have to take this to appropriations? The answer is no.

Representative Ruby: Why the \$5 million? Is that arbitrary? Have you done any calculations that \$2 million or \$3 million would be sufficient?

Humann: There is not anything scientific behind that amount. Historically, increments of the allotments have been \$5 million at a time. It has taken us a while to use that money up and get close to the \$10 million mark. We are just continuing to go with the \$5 million increment. It is hard to predict whether the additional \$5 million will go through the next biennium or will it last longer? It just depends on the deal flow that we're going to end up having in the state in the next few years.

For 2012, we did one loan for \$250,000 and five investments for \$600,000. For just the year 2012, we did only \$1 million. Early on in this fund, we were doing more deals. What has happened around that state is that there have been other venture capital groups that have formed throughout the state. This is a great leveraging tool for the ND Development Fund to be able to promote the small businesses because it splits risks between the North Dakota Development Fund and the Bank of North Dakota.

Chairman Keiser: Any additional questions for Mr. Humann? Seeing no questions, is there anyone else who would like to talk to us? Dean?

Dean Reese, CEO of ND Development Fund. (19:20) The North Dakota Development Fund manages the New Venture Capital Program. We have done that since 2008.

A lot of these are new companies at that early stage. That is the riskiest type of funding that you can be involved with. A lot of times, we are in subordinate positions. In the event that the company is not successful, that position allows the lead bank or lead lender to come in on those situation, which is very good. They feel more secure because they have our dollars behind them in a subordinate position, and they have a first position on the collateral. The New Venture Capital Program and North Dakota Development Fund are not large enough to provide the full funding for the request, and that is where the lead lender is very important. We work with the lead lender on a shared or subordinate position, and that allows the lead bank to come in with their money, and that allows the startup to create jobs, build buildings, and so forth. The New Venture Fund is not tied to new jobs as the Development Fund, but obviously it creates more opportunities for the citizens of North Dakota.

The more programs you have involved in providing funding to the startup, the more you spread the risk and leverage. We try to use both the North Dakota Development Fund and the New Venture Fund on a 50/50 basis.

(21:10) When I first started, many times it was only state funds in the project. We've learned that if we're putting in dollars from the state, we also want private dollars to come in. We require them to put dollars in so that they have a stake in the game. It works well because it leverages those dollars and allows us to have more access and funding dollars to help with those projects. We probably went over the dollar amount we were authorized, but we got payback during that time, so it has worked very well. It has changed sometimes, based on the projects, based on the dollars that the banks have. If it is a good deal, they keep those projects in the bank rather than partnering with the other funds or with other programs in the state. It is nice having the ability to inform people that we have two programs that we can utilize to help get the project in the communities in North Dakota.

Chairman Keiser: (22:40) Questions for Mr. Reese?

Representative Gruchalla: Do you keep a separate file for your management costs for the fund?

Reese: Yes, we do. When we had the opportunity, based under the Century Code, which allowed the Development Fund to be one of the third party management or an outside source, we came to an agreement with the Bank of North Dakota. We have an excellent relationship with the Bank of North Dakota. We probably collect enough in commitment fees when we do these to cover the costs of what we do to manage it. Our fee is pretty minimal based on the dollar amounts we manage. The Development Fund is already in a lot of the projects, so we're already looking at it based on our staff and so forth. We do keep a separate accounting, and we send it to the bank each month, the balances, so we are dollar-for-dollar the same. We also send a report at year end showing the amount of interest we've collection and commitment fees. We give a breakdown each year showing what those costs are. Right now, the Development Fund manages 8 programs or funds. I have a separate bank account for each one. Records are kept to indicate specifics of dollars tied to a specific program.

Chairman Keiser: Further questions? Anyone else here to testify in support of HB 1078? Anyone here to testify in opposition to HB 1078? Seeing no one, we will close the hearing on HB 1078.

(24:37) What are the wishes of the committee?

Representative Kasper: Motion to do pass

Representative Kreun: Seconded the motion

Representative Becker: In order to give it a yes vote, I would like more information and time to scrutinize it. Am I able to abstain from voting?

Chairman Keiser: In the North Dakota system, committee members cannot abstain. In some states, members can take a walk and just disappear and not vote. We are a citizen legislature, and our requirement is that we listen and then we vote. You can certainly vote no if you do not know enough about the issue at hand, so that is an option. Further discussion? Seeing none, we have a motion for a "do pass" on HB 1078. We will ask the clerk to take the roll call vote.

Roll call vote on the motion to do pass: 13 yes; 1 no; 1 absent and not voting. Motion carries.

Chairman Keiser: We talk a lot about legislative history and the fact that when you have the opportunity to serve many years....I was here when we passed this legislation, so I've heard this issue over a long period of time, and that's an advantage to having served over many years.

Committee adjourned.

Bill will be carried by Representative Kreun.

Date: ~~1078~~ 1-9-2013

Roll Call Vote #: 1

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1078

House Industry, Business, and Labor Committee

Legislative Council Amendment Number —

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment
 Rerefer to Appropriations Reconsider Consent Calendar

Motion Made By Kasper Seconded By Kreun

Representatives	Yes	No	Representatives	Yes	No
Chairman George Keiser	✓		Rep. Bill Amerman	✓	
Vice Chairman Gary Sukut	✓		Rep. Joshua Boschee	✓	
Rep. Thomas Beadle	✓		Rep. Edmund Gruchalla	✓	
Rep. Rick Becker		✓	Rep. Marvin Nelson	✓	
Rep. Robert Frantsvog	✓				
Rep. Nancy Johnson	✓				
Rep. Jim Kasper	✓				
Rep. Curtiss Kreun	✓				
Rep. Scott Louser	✓				
Rep. Dan Ruby	✓				
Rep. Don Vigesaa	✓				

Total Yes 13 No 1

Absent 1 Amerman

Floor Assignment Kreun

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1078: Industry, Business and Labor Committee (Rep. Keiser, Chairman)
recommends **DO PASS** (13 YEAS, 1 NAYS, 1 ABSENT AND NOT VOTING).
HB 1078 was placed on the Eleventh order on the calendar.

2013 SENATE INDUSTRY, BUSINESS AND LABOR

HB 1078

2013 SENATE STANDING COMMITTEE MINUTES

Senate Industry, Business and Labor Committee Roosevelt Park Room, State Capitol

HB 1078
February 20, 2013
Job Number 19232

Conference Committee

Committee Clerk Signature

Explanation or reason for introduction of bill/resolution:

Relating to the investment of funds by the Bank of North Dakota

Minutes:

Testimony Attached

Bob Humann, Senior VP of lending for the Bank of North Dakota: Written Testimony Attached (1). (1:20-10:00)

Senator Sinner: Asked if the money comes out of deposits or equity.

Bob: Said it is equity money.

Senator Andrist: Asked if the fifteen million dollars was a cap and do you get any pay back.

Bob: Said the fifteen million dollars is a cap and it should last another four years. He commented about wanting to spur economic development and to give them another tool.

Senator Murphy: Asked for him to explain the North Dakota Development Fund.

Bob: Said back in 2005 there wasn't a lot of dollars available for the fund so they decided to create a separate fund called the New Venture Capital Program and used the banks equity. It was primarily to support the ALIEN project that was going to be located in Fargo. At that time there was five million dollars set aside for the New Venture Capital Program. (10:00-12:00)

Senator Sinner: Asked if it stated a maximum.

Bob: Said that there is no maximum stated but at the bank they hold it at three hundred thousand dollars.

Chairman Klein: Said so there is a back stop?

Bob: Said yes there is a back stop.

Dean Reese, North Dakota Development Fund for the Bank of North Dakota: Said the fund has been around since 1991. They get their appropriations through the legislative process. They have received approximately twenty-seven million in appropriations since the fund was created. In June it should be over one hundred million. When the legislators created the fund they wanted it to be a revolving loan fund, it has turned into that. They have eight programs with the fund that they oversee. (13:15-19:10)

Informational time about the fund and how it works (19:15-27:35)

2013 SENATE STANDING COMMITTEE MINUTES

Senate Industry, Business and Labor Committee
Roosevelt Park Room, State Capitol

HB 1078
February 25, 2013
Job Number 19422

Conference Committee

Committee Clerk Signature

Eva Lutelt

Explanation or reason for introduction of bill/resolution:

Relating to investment funds by the Bank of North Dakota

Minutes:

Discussion and Vote

Chairman Klein: Explained the bill.

Comments followed

Senator Andrist: Moved a do pass.

Senator Sinner: Seconded the motion.

Roll Call Vote: Yes - 7 No - 0 Absent - 0

Floor Assignment: Senator Sorvaag

**2013 SENATE STANDING COMMITTEE
 ROLL CALL VOTES
 BILL/RESOLUTION NO. 1078**

Senate Industry, Business, and Labor Committee

Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment
 Rerefer to Appropriations Reconsider

Motion Made By Senator Andrist Seconded By Senator Sinner

Senators	Yes	No	Senator	Yes	No
Chairman Klein	x		Senator Murphy	x	
Vice Chairman Laffen	x		Senator Sinner	x	
Senator Andrist	x				
Senator Sorvaag	x				
Senator Unruh	x				

Total (Yes) 7 No 0

Absent 0

Floor Assignment Senator Sorvaag

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1078: Industry, Business and Labor Committee (Sen. Klein, Chairman) recommends **DO PASS** (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1078 was placed on the Fourteenth order on the calendar.

2013 TESTIMONY

HB 1078

HB 1078
① 1/9/13

TESTIMONY TO THE
HOUSE INDUSTRY, BUSINESS AND LABOR COMMITTEE
HOUSE BILL 1078
BOB HUMANN – SVP OF LENDING
BANK OF NORTH DAKOTA
JANUARY 9, 2013

House Bill 1078 increases the maximum amount from \$10 million to \$15 million that the Bank of North Dakota may have outstanding in the New Venture Capital Program. This program consists of investments and subordinate loans to North Dakota businesses that are early-stage or expanding. This program began in 2003 with a \$5 million ceiling and was increased by an additional \$5 million in 2005. The funds for this program are provided by the bank. The investments and loans are serviced by the North Dakota Development Fund.

As of December 31, 2012, the bank has \$1.5 million of availability under the \$10 million ceiling. The additional \$5 million will provide availability to ensure that this program is available through the next biennium to handle North Dakota's strong economic growth.

Your approval of the proposed \$5 million increase is recommended.

TESTIMONY TO THE
SENATE INDUSTRY, BUSINESS AND LABOR COMMITTEE
~~HOUSE~~ SENATE BILL 1078
BOB HUMANN – SVP OF LENDING
BANK OF NORTH DAKOTA
FEBRUARY 20, 2013

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