Vermont's False Fiscal Dilemma

by Michael Taub

The September 7th article in the Times Argus by Peter Hirschfield titled *"State finances: Bonding amounts may drop, affecting infrastructure repairs"* presents a false dilemma for Vermonters. We are told we must reduce spending on needed infrastructure and public safety or risk the loss of Vermont's AAA bond rating. This is akin to another false choice we are told we have to make every year when the legislature convenes - the choice of raising taxes or cutting spending to balance the budget. We hear about $20 million budget "holes" that have to be filled, and hard choices that have to be made between programs like the Earned Income Tax Credit and early childhood education. Now it's our core infrastructure we're being told we can't afford – roads, bridges, schools, energy improvements, wastewater treatment, cleaning up Lake Champlain.

The article stated that we will need to cut 37%, or $52 million, in capital spending over two years, out of $160 million total spending. Vermont is currently paying $74 million annually for debt service on $550 million in general obligation loans, a debt load characterized as 'considerable.' But there is more to the story. During fiscal 2013, Vermont's average end-of-day balance was over $357 million – that's the money we have deposited in banks, deposits that are collateralized to keep them insured. We paid over $700,000 in fees to the large banks like TD Banknorth for this service. In the last 10 fiscal years we paid over $225 million in interest on General Obligation (G.O.) bonds, and the 2012 Capital Debt Affordability Advisory Committee (CDAAC) report estimates this will explode to $272 million over the next ten years. Interest on bonds for local projects is not included in this total – this is just for state capital spending.

This fantastic amount of money is paid to Wall Street banks for the privilege of using what is essentially our own money. In addition, because of the fractional reserve system, the banks can make over $3.5 BILLION in loans by lending out these deposits, which in turn creates new deposits, which are also loaned out – creating new money through the banking system and earning lots and lots of interest, all because of Vermont's public fund deposits.

This incredibly expensive system is also surprisingly risky. Should the big banks fail, current Chapter 11 bankruptcy law now gives first priority to holders of the bank's repurchase agreements and derivatives, whose rights to repayment now come before depositors. The world derivative market is currently $1.2 QUADRILLION, or 20 times the size of the world's economy. There simply isn't enough money in the world to pay the derivative holders, let alone the bank's depositors – we are now legally considered unsecured creditors by the banking industry. If you think the FDIC will somehow bail us all out, think again - the Fund Balance at the FDIC was only $75 Billion at the end of 2012.[i] According to a recent study done by Harvard professor Mark J. Roe and published in the Stanford Law Review[ii], the financial institutions that hold the derivatives can now seize the collateral we imagine is keeping our state deposits secure in payment for their losses. This fantastic risk is perhaps the most compelling reason to explore alternatives to our current financial management system at the state level.

There is a third choice to the false dilemma the bond rating agencies who represent the big banks from Wall Street present - we can create a public bank and harness the power of Vermont's public funds to benefit all Vermonters. A public bank would hold and manage Vermont's taxpayer funds, resulting in substantial savings in interest and fees. Like the successful public banks in North Dakota, Germany, India, and Brazil, a Vermont state bank can generate new income for the state, as well as provide a stable source of credit for our towns, students, homeowners, and small businesses.

This is because the payments on the lending it does would benefit the citizens of the state, not private bank shareholders or private bondholders. It would also be much safer than the large private banks that are currently overexposed to the international derivatives market. The bond rating that state administrators think is so important to our future holds less of an influence over our borrowing ability and the long-term costs of financing needed public infrastructure when we are borrowing from ourselves instead.

Vermonters can learn more about public banking and other New Economy ideas during Vermont's New Economy Week, October 10-20. This will be a statewide discussion about how to create an economy that works for the people, the planet and for Vermont. Currently, Vermonters in 22 towns are circulating information about public banking, local investment, slow money, cooperatives, worker owned enterprises, new forms of measurement, and are organizing local events. The kickoff will be October 10th and 11th, when Michael Shuman, author of ***Local Dollars, Local Sense***, speaks at Chandler in Randolph and at the Kellogg Hubbard Library in Montpelier.

Michael Taub is a member of Vermonters for a New Economy, a state-wide grassroots movement working to create and demonstrate new economic possibilities for Vermont. More information about New Economy Week can be found on the web site - (www.vtneweconomy.org).

[i] Federal Deposit Insurance Corporation Annual Report 2012. Financial Statements and Notes. (http://www.fdic.gov/about/strategic/report/2012annualreport/chpt4-01.html)
[ii] Mark J. Roe, *The Derivatives Market's Payment Priorities as a Financial Crisis Accelerator.* Stanford Law Review 539, March 6, 2011.