**HOUSE OF REPRESENTATIVES**
**COMMITTEE ON**
**FINANCIAL SERVICES**
**BILL RESEARCH & ECONOMIC IMPACT STATEMENT**

**BILL #**: HB 823

**RELATING TO**: Financial Matters

**SPONSOR(S)**: Representative Gay

**STATUTE(S) AFFECTED**: s. 18.10, F.S.

**COMPANION BILL(S)**: SB 988 (s)

**ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE**:
(1) FINANCIAL SERVICES YEAS 11 NAYS 0
(2) GOVERNMENTAL OPERATIONS
(3) FINANCE & TAXATION
(4)
(5)

---

I. SUMMARY:

The Department of Insurance, Division of Treasury operates the state's cash management and investment programs, which involve collecting funds from various state revenue sources, disbursing funds to pay state expenses, and investing the excess funds to maximize value. The bill permits, rather than mandates, that state revenues not used for disbursements be made available for deposit in banks or savings and loans. The former mandatory deposit rule gave the depositories primary discretion to determine the level of excess funds which became available for investment. The bill transfers this discretion to the Treasurer by granting authority to invest all funds not disbursed and not deposited, instead of waiting to invest only funds not accepted by the depositories.

The bill expands the investment options available to the Treasurer to an additional grade of corporate and government bonds, to longer term and convertible corporate bonds, and to foreign bonds.

The Committee on Financial Services adopted one amendment that is explained in Section VI below.

II. SUBSTANTIVE RESEARCH:

A. PRESENT SITUATION:

The State Treasurer is required under Art. IV, § 4, Fla. Const., to keep all state funds and to disburse state monies only upon the order of the Comptroller. Section 18.10, F.S., directs the Treasurer to deposit state monies into qualified banks or savings and loan associations which meet the definition of "public depositories" in chapter 280, F.S. The Treasurer is under a duty to keep these monies fully invested or deposited, as the cash disbursement needs of the state allow, for maximum earnings and benefits to the state. Any funds not required for disbursements must be placed in qualified public depositories, so long as they agree to pay interest on these deposits at a minimum rate established by the Treasurer, pursuant to statute. If public depositories are unwilling to receive all or part of the funds and pay the Treasurer's minimum rate, the Treasurer is then authorized to invest the funds in specific securities. Earnings from these investments must be credited to the General Revenue Fund.

Section 20.13, F.S., designates the head of the Department of Insurance (hereinafter "DOI") as the Treasurer. The Division of Treasury in the DOI is responsible for implementing the responsibilities of the Treasurer in Chapter 18, F.S., which include the investment duties. The division contracts with outside investment managers to invest the excess funds which, according to the division, average $9 billion in daily accounts. The investment managers generally must wait until a specific time of the day, when the public depositories have determined their deposits, before making investment decisions.

Section 18.10(2), F.S., restricts these investments to specific securities, or, to securities that meet general credit criteria, known as "investment grade" securities. These criteria are established through ratings from three national organizations, Standard and Poor's, Moody's and Fitch's. Their ratings are generally represented as: (i) "AAA" - the highest most secure rating, extremely strong investment potential; "AA" - very strong security which differs from AAA by a small degree; "A" - strong but susceptible to adverse economic conditions; and "BBB" - adequate investment potential with more susceptibility to adverse economic conditions. Securities rated in classifications lower than BBB are not considered investment grade. When the division's money managers invest in government-issued or corporate-issued securities, they are restricted under s. 18.10(2), to only those issuances with ratings in one of the three highest classifications. Additionally, present law restricts the Treasurer's authority to purchase state and local government bonds (also known as municipals) for the purpose of compliance with federal arbitrage restrictions on tax exempt security transactions. This law prohibits issuers of tax exempt securities from investing the proceeds of the sale to obtain higher returns than were paid on the tax exempt securities. Under section 18.10(2), the Treasurer can purchase municipals with proceeds of the state's tax exempt securities, and thereby comply with the federal arbitrage requirement.

B. EFFECT OF PROPOSED CHANGES:

The Treasurer will have the discretion under this bill to determine the amounts of nondisbursed state funds deposited into public depositories, or invested. Public depositories will no longer influence investment strategy by their decision to decline deposits, which allows the Treasurer an opportunity to optimize returns. The bill allows the Treasurer additional investment options by adding BBB-rated securities, and longer-term corporate bonds as qualified investments. According to the division, investment consultants will identify BBB-rated securities that offer attractive risk/return profiles, with stronger yields from longer-term corporate and intermediate local investments. The Treasurer is authorized to purchase municipal bonds for purposes other than compliance with federal arbitrage restrictions, and is authorized to invest in foreign, primarily European, bonds denominated in U.S. dollars to eliminate exchange risk. These bonds, known in the industry as "Yankee bonds," must meet minimum criteria, including registration with the Securities and Exchange Commission (SEC). Corporate convertible debt also qualifies for the first time as an investment vehicle if minimum criteria are met.

C. APPLICATION OF PRINCIPLES:

1. <u>Less Government:</u>

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

No.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

No. However, the Treasurer will have broader discretion to make investment determinations, without waiting on responses from banks or savings and loans.

(3) any entitlement to a government service or benefit?

No.

b. If an agency or program is eliminated or reduced:

Not applicable.

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

Not applicable.

(2) what is the cost of such responsibility at the new level/agency?

Not applicable.

(3) how is the new agency accountable to the people governed?

Not applicable.

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

No.

b. Does the bill require or authorize an increase in any fees?

No.

c. Does the bill reduce total taxes, both rates and revenues?

No. However, see section 2.a above.

d. Does the bill reduce total fees, both rates and revenues?

No.

e. Does the bill authorize any fee or tax increase by any local government?

No.

3. Personal Responsibility:

a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

No.

b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

No.

4. Individual Freedom:

a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

No.

b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

No.

5. Family Empowerment:

a. If the bill purports to provide services to families or children:

No.

(1) Who evaluates the family's needs?

Not applicable.

(2) Who makes the decisions?

Not applicable.

(3) Are private alternatives permitted?

No.

(4) Are families required to participate in a program?

No.

(5) Are families penalized for not participating in a program?

No.

b. Does the bill directly affect the legal rights and obligations between family members?

No.

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

Not applicable.

(2) service providers?

Not applicable.

(3) government employees/agencies?

Not applicable.

D. SECTION-BY-SECTION RESEARCH:

**Section 1.** Amends subsection (2) in s. 18.10, F.S., to revise requirements for deposit and investment of state funds not required for disbursement. The bill makes it permissive, rather than mandatory, for the Treasurer to deposit state funds not needed to meet the disbursement needs of the state, into qualified public depositories. The bill makes all remaining funds (not disbursed and not deposited) available for investment in designated securities. Previously, funds became available for investment only when the depositories declined to accept the state funds under terms prescribed by the Treasurer.

The bill revises criteria for two securities in which the Treasurer may invest, corporate bonds and government bonds, and establishes criteria for investing in two new securities. Criteria for corporate bonds are revised to remove restrictions allowing purchase of intermediate term bonds only (maturity of 10 years or less), which effectively authorizes investment in longer term corporate bonds (maturity beyond 10 years). The bill also authorizes investment in corporate bonds which at least two of the national rating organizations have rated in one of the four highest rating classifications. Previously, only corporate bonds rated in one of the three highest classifications qualified. The bill revises criteria for investment in state and local government bonds (municipals) to those which meet the same rating criteria as for corporate bonds, except, if the municipal bonds have been rated by only one service, the bill authorizes the Treasurer to invest in AAA or AA rated bonds only, the two highest classifications. The bill allows more active investment in municipals by removing restrictions allowing the purchase of municipals solely to comply with federal investment requirements.

Criteria are established for investment in two additional securities -- bonds of foreign-owned corporations, and U.S. corporate bonds that are convertible into stock. The bill authorizes investments in foreign bonds which are: (i) denominated in U.S. dollars; (ii) registered with the U.S. SEC; and (iii) rated as long-term bonds by at least two of the national organizations in one of the four highest classifications, except if the bonds are rated by only one organization, the rating must be in one of the two highest classifications. The bill authorizes investment in convertible bonds if: (i) the issuing corporation is domiciled in the U.S.; and (ii) the same rating criteria is met as for foreign bonds.

**Section 2.** Provides that the bill shall take effect on July 1, 1997.

III. FISCAL RESEARCH & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

After an independent study of its investment practices by a consultant, the division estimates that implementation of the discretion and investment strategies authorized in the bill should increase returns from investments between $1.7 million to $2 million per year.

3. Long Run Effects Other Than Normal Growth:

Increased returns in Treasury investments go directly in the General Revenue Fund, which may reduce the total revenue demands on the state.

4. Total Revenues and Expenditures:

See section A.2 above.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

Public depositories will have less discretion in electing to receive deposits of state funds. According to the department, depositories generally receive a relatively small percentage of the available funds for deposit. Deposits will continue if the bill is enacted, at an undetermined level.

2. Direct Private Sector Benefits:

   None.

3. Effects on Competition, Private Enterprise and Employment Markets:

   None.

D. FISCAL COMMENTS:

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

B. REDUCTION OF REVENUE RAISING AUTHORITY:

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

V. COMMENTS:

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

At its meeting on March 26, 1997, the Committee on Financial Services adopted one amendment to the bill which reinserts existing law and continues the requirement that state funds not used for disbursements be deposited into public depositories.

VII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

| Prepared by: | Legislative Research Director: |
|---|---|
| E. LEON JACOBS, JR. | STEPHEN HOGGE |