

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 871 CS

Investment of Public Funds

SPONSOR(S): Bilirakis

TIED BILLS:

IDEN./SIM. BILLS: SB 1998

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) <u>Economic Development, Trade & Banking Committee</u>	<u>15 Y, 0 N, w/CS</u>	<u>Sheheane</u>	<u>Carlson</u>
2) <u>Finance & Tax Committee</u>	<u></u>	<u></u>	<u></u>
3) <u>Commerce Council</u>	<u></u>	<u></u>	<u></u>
4) <u></u>	<u></u>	<u></u>	<u></u>
5) <u></u>	<u></u>	<u></u>	<u></u>

SUMMARY ANALYSIS

The bill allows the Chief Financial Officer and units of local government to deposit certain funds with qualified public depositories under the following conditions:

- The funds must be initially deposited through a qualified public depository, as defined in s. 280.02, F.S., selected by the Chief Financial Officer or unit of local government.
- The selected depository must arrange for deposit of the funds in certificates of deposit in one or more federally insured banks or savings and loans associations, wherever located, in the account of the state or unit of local government.
- The full amount of principle and accrued interest of each certificate of deposit must be insured by the Federal Deposit Insurance Corporation.
- The selected depository is to act as custodian for the state or unit of local government with respect to such certificates of deposit issued for its account.
- At the same time the state's funds are deposited and the certificates of deposit are issued, the selected depository receives an amount of deposits from customers of other federally insured financial institutions, wherever located, equal to or greater than the amount of the funds initially invested by the Chief Financial Officer or unit of local government through the selected depository.

The bill will take effect on July 1, 2005.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

The bill does not appear to implicate any of the House Principles.

B. EFFECT OF PROPOSED CHANGES:

Current Situation

Public Deposits

Section 280.02, F.S., defines a “public deposit” as the moneys of the state or any county, school district, community college district, special district, metropolitan government, or municipality, including agencies, boards, bureaus, commissions, and institutions of any of the foregoing, or of any court, and includes the moneys of all county officers, including constitutional officers, that are placed on deposit in a bank, savings bank, or savings association and for which the bank, savings bank, or savings association is required to maintain reserves.

A public deposit includes, but is not limited to, time deposit accounts, demand deposit accounts, and nonnegotiable certificates of deposit. Moneys in deposit notes and in other nondeposit accounts such as repurchase or reverse repurchase operations are not considered public deposits. Securities, mutual funds, and similar types of investments are not considered public deposits.

Qualified Public Depositories

A “qualified public depository” is any bank, savings bank, or savings association that: is organized and exists under the laws of the United States, the laws of this state or any other state or territory of the United States; has its principal place of business in this state or has a branch office in this state which is authorized under the laws of this state or the United States to receive deposits in this state; has deposit insurance under the provision of the Federal Deposit Insurance Act, as amended, 12 U.S.C. ss. 1811 et seq; has procedures and practices for accurate identification, classification, reporting, and collateralization of public deposits; meets all the requirements of chapter 280, F.S., and; has been designated by the Chief Financial Officer as a qualified public depository.¹

Collateral for Public Deposits

The Chief Financial Officer determines the collateral requirements and collateral pledging level for each qualified public depository following procedures established by rule. A qualified public depository may not accept or retain any public deposit which is required to be secure unless it has deposited with the CFO eligible collateral within specific parameters, including minimum required collateral of \$100,000. A qualified public depository may be required to return public deposits to governmental units and be suspended, disqualified or subject to administrative penalty as provided in ss. 280.051 or 280.054, F.S., for failure to maintain required collateral.

Public Deposits Secured

All public deposits are considered secure as provided in chapter 280, F.S., when public depositors comply with the provisions of the chapter. Public deposits are to be made in a qualified public depository unless exempted by law. Public funds cannot be deposited directly or indirectly in negotiable certificates of deposit.

¹ See s. 280.02, F.S.

The following are exempt from requirements of and protection under chapter 280, F.S., : public deposits deposited in a bank or savings association by a trust department or trust company which are fully secured under trust business laws; moneys of the System Trust Fund, as defined in s. 121.021 (36), F.S.; public deposits held outside the country; wire transfers and transfers of funds solely for the purpose of paying registrars and paying agents; and public deposits which are fully secured under federal regulations.

Federal Deposit Insurance Corporation

Section 330.15 of the FDIC's regulations (12 C.F.R. s. 330.15) governs the insurance coverage of "public unit" accounts. For deposit insurance purposes, the term "public unit" includes a state, county, municipality, or "political subdivision" thereof. Under section 330.15, the "official custodian" of the funds belonging to the public unit is insured as the depositor.

The insurance coverage of public unit accounts depends upon:

- the type of deposit; and
- the location of the insured depository institution.

All "time and savings deposits" owned by a public unit and held by the same official custodian in an insured depository institution within the state in which the public unit is located are added together and insured up to \$100,000. Separately, all "demand deposits" owned by a public unit and held by the same official custodian in an insured depository institution within the state in which the public unit is located are added together and insured up to \$100,000.

The insurance coverage of public unit accounts is different if the depository institution is located outside the state in which the public unit is located. In that case, all deposits owned by the public unit and held by the same official custodian are added together and insured up to \$100,000. Time and savings deposits are not insured separately from demand deposits.

Deposit insurance coverage cannot be increased by dividing funds among several putative official custodians who lack plenary authority over such funds. Likewise, coverage cannot be increased by dividing funds among several accounts controlled by the same official custodian for the same public unit.

Certificate of Deposit Account Registry Service (CDARS)

The Certificate of Deposit Account Registry Service is a deposit placement service run by Promontory Registry Service that allows Federal Deposit Insurance Corporation (FDIC) insured institutions to accept deposits greater than \$100,000, including principal plus interest, and up to \$10 million for a single depositor, while still maintaining FDIC insurance on that deposit. Once a depositor places the money in the institution, certificates of deposit (CD's) of up to \$100,000 are issued to other network banks located anywhere in the country. These banks then issue CD's of the same amount back to the bank where the original deposit was made. As a result, the money comes back to the state and the local bank has the benefit of using the full amount of the deposit for local lending. The system is based on a reciprocal relationship between network banks, but the customer maintains a single relationship with the original bank in which the funds were deposited. Currently, there are over 600 network banks nationwide and 23 network banks in Florida. To become a member bank, the bank must be well capitalized and have FDIC insurance.

The CDARS program allows for deposits into qualified public depositories up to \$10 million while maintaining FDIC insurance on the deposit, thus eliminating the need for qualified public depositories to deposit certain eligible collateral with the CFO.

CDARS Facts

The CDARS program was created by Promontory Interfinancial Network, an Arlington, Virginia based firm which employs approximately 90 people. The firm was established in July 2002, and the CDARS product was established in January 2003. CDARS is endorsed by the American Bankers Association. Currently, several states are using the CDARS system, including Alaska, Connecticut, Georgia, Tennessee, Nebraska, Colorado, and Illinois, along with many others.

Proposed Changes

The bill codifies the "CDARS" program in law by permitting the Chief Financial Officer to deposit state funds not needed to meet the disbursement needs of the state with the following conditions:

- The funds must be initially deposited through a qualified public depository, as defined in s. 280.02, F.S., selected by the Chief Financial Officer.
- The selected depository arranges for deposit of the funds in certificates of deposit in one or more federally insured banks or savings and loans associations, wherever located, in the account of the state.
- The full amount of principal and accrued interest of each certificate of deposit must be insured by the Federal Deposit Insurance Corporation.
- The selected depository is to act as custodian for the state with respect to such certificates of deposit issued for its account.
- At the same time the state's funds are deposited and the certificates of deposit are issued, the selected depository receives an amount of deposits from customers of other federally insured financial institutions, wherever located, equal to or greater than the amount of the funds initially invested by the Chief Financial Officer through the selected depository.

The bill also authorizes a unit of local government to deposit any portion of surplus public funds under identical conditions.

The bill exempts deposits made pursuant to ss. 17.57 and 218.45, F.S., from the collateral requirements of ch. 280, F.S.

FDIC Approval

In a letter dated July 29, 2003, the Federal Deposit Insurance Corporation agreed that deposits placed through the CDARS system would be insured on a pass-through basis under the FDIC's rules on the insurance coverage of agency or custodial accounts.

How CDARS Works

Public funds are deposited in a relationship bank. While the lump sum deposit remains in the bank, dollar- for-dollar FDIC coverage in CD's up to \$100,000 is exchanged with at least 11 member banks around the country through matches made at the Bank of New York, which acts as a clearinghouse for the CDARS program.

For a bank to accept public deposits in Florida, it must be a qualified public depository as defined under s. 280.02, F.S.

Example:

Sarasota School Board deposits \$2 million in Bank of Sarasota, who is a member bank for the CDARS program. The \$2 million deposit remains in the Bank of Sarasota, but is broken into various CD

amounts up to \$100,000 (principle plus interest) and reciprocal FDIC coverage is exchanged with member banks.

The rate of return on the public deposit is typically higher than would be seen on other deposits. The higher rate is a result of increased competition for the deposits and because the bank does not have the expense associated with pledging collateral.

Early Withdraw Penalty:

If the depositor seeks to withdraw its deposit early, the relationship bank, or the bank where the deposit is originally made, has two options:

1. It can offer a loan to the depositor against the total deposit to avoid the early termination fee; or
2. The relationship bank may call in the CD's from the member banks and pay the fee (50% of the interest earned on the CD) to the member bank that is losing the funds due to the early termination of the CD. The relationship bank determines whether or not to pass the fee to the depositor.

Bank Failure:

The depositor will always be able to recover the full amount of the deposit. If the relationship bank should fail, the FDIC would take over the relationship bank and hold the CD's until they mature.

If a member bank fails, the FDIC would go to the Bank of New York and seize the CD's issued by the failed member bank and do one of the following:

1. Sell the bank and therefore its liabilities, or
2. Sell the CD's in bulk as demand CD's.

Accounting

The governmental unit depositing funds into a single qualified public depository will be considered to have a deposit in that qualified public depository alone. It would not be necessary to record deposits for all sharing depositories.

C. SECTION DIRECTORY:

Section 1: Amends s. 17.57, F.S., relating to deposits and investments of state money to provide additional authorization for the Chief Financial Officer to invest state funds under certain conditions.

Section 2: Amends s. 218.415, F.S., relating to local government investment policies to provide additional authorization for local governments to invest surplus funds under certain conditions.

Section 3: Amends s. 280.03, F.S., to clarify that funds placed according to the bill's provisions are exempt from the security requirements of Chapter 280, F.S.

Section 4: Provides that the act will take effect July 1, 2005.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

The bill appears not to have an impact on state government revenues.

2. Expenditures:

The bill appears not to have an impact on state government expenditures.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

The bill appears not to have an impact on local government revenues.

2. Expenditures:

The bill appears not to have an impact on local government expenditures.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill may increase competition in the CD market by increasing demand through the CDARS program for secured deposits of public funds.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds. This bill does not reduce the percentage of a state tax shared with counties or municipalities. This bill does not reduce the authority that municipalities have to raise revenues.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

No exercise of rule-making authority is required to implement the provisions of this bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES

In the meeting on March 11, 2005, the Economic Development, Trade and Banking Committee adopted a strike-all amendment to the bill. The amendment clarifies that the funds placed by the state or local government are considered deposits, not investments. The amendment also clarifies that funds placed according to the bill's provisions are exempt from the security requirements of Chapter 280, F.S., which require collateral for public deposits.