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GOVERNMENT FUNDS: INVESTMENTS

Senate Bill 664 (Substitute H-3) First Analysis (12-10-97)

Sponsor: Sen. Bill Bullard
Senate Committee: Finance
House Committee: Local Government

THE APPARENT PROBLEM:

Legislation has been introduced to update Public Act 20 of 1943, which regulates how local units of government may invest their surplus funds. The legislation has been developed out of discussions among municipal finance officers, local treasurers, bonding attorneys, and banking and investment representatives.

THE CONTENT OF THE BILL:

The bill would amend Public Act 20 of 1943, which regulates the investment of surplus funds by local units of government, in order, among other things, to require each public corporation to adopt an investment policy; to impose requirements on financial intermediaries, brokers, and dealers who want to purchase or trade the funds of a public corporation; and to update the investment options for public corporations.

The term "public corporation" would mean a county, city, village, township, port district, drainage district, special assessment district, or metropolitan district of this state, or a board, commission, or another authority or agency created by or under an act of the legislature of the state. The term "investment officer" would mean the treasurer or other person designated by statute or charter to act as the investment officer. In the absence of a designation by statute or charter, the governing body would designate the investment officer. The term "funds" would mean the money of a public corporation, the investment of which was not otherwise subject to a public act of the state or bond-authorizing ordinance or resolution of a public corporation that permits investment in fewer than all of the options in Public Act 40 or imposes one or more conditions on a permitted investment.

Investment Policies. Not more than 180 days after the end of a public corporation's first fiscal year that ends after the effective date of the bill, a governing body of a public corporation would have to adopt an investment policy (in consultation with its investment officer). The

policy would have to include, at a minimum, all of the following:

-- A statement of the purpose, scope, and objectives of the policy, including safety, diversification, liquidity, and return on investment.

-- A delegation of authority to make investments.

-- A list of authorized investment instruments. If the policy authorized an investment in mutual funds, it would have to indicate whether the authorization was limited to securities whose intention was to maintain a net asset value of \$1 per share or also included securities whose net asset value per share could fluctuate periodically.

-- A statement concerning safekeeping, custody, and prudence.

A governing body that had already, as of the bill's effective date, adopted an investment policy that substantially complies with the minimum requirements of the bill would not be in violation as long as that policy remained in effect.

Financial Intermediaries, etc. Before executing an order to purchase or trade the funds of a public corporation, a financial intermediary, broker, or dealer would have to be provided with a copy of the public corporation's investment policy and would have to 1) acknowledge receipt of the policy; and 2) agree to comply with the terms of the policy regarding the buying or selling of securities.

Permitted Investments. The bill would rewrite the current investment provisions. A governing body could by resolution authorize its investment officer to invest the funds in:

-- bonds, securities, and other obligations of the United States or an agency or instrumentality of the United States

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(without the current restriction that the principal and interest must be fully guaranteed);

-- repurchase agreements consisting of instruments listed above;

-- certificates of deposit, savings accounts, deposit accounts, or depository receipts of a financial institution (as now);

-- commercial paper rated at the time of purchase within the two highest (rather than three highest) classifications established by not less than two standard rating services and that matures not more than 270 days after the date of purchase, without the current requirement that not more than 50 percent of any fund can be invested in commercial paper at any time;

-- bankers' acceptances of United States banks (as now);

-- obligations of this state or any of its political subdivisions that at the time of purchase are rated as investment grade by at least one standard rating service;

-- mutual funds registered under the federal Investment Company Act of 1940 with authority to purchase only investment vehicles that are legal for direct investment by a public corporation;

-- obligations cited in the paragraphs above if purchased through an interlocal agreement under the Urban Cooperation Act;

-- investment pools organized under the Surplus Funds Investment Pool Act; and

-- investment pools organized under the Local Government Investment Pool Act.

The bill would also specify that assets acceptable for pledging to secure deposits of public funds would be limited to assets authorized for direct investment as provided in the paragraphs above and would eliminate the list of such acceptable assets.

Mutual Funds. The bill would specify that a mutual fund would not be disqualified as a permissible investment solely by reason of any of the following: 1) the purchase of securities on a when-issued or delayed delivery basis; 2) the ability to lend portfolio securities as long as the mutual fund receives collateral at all times equal to at least 100 percent of the value of the securities loaned; or 3) the limited ability to borrow and pledge a like portion of the portfolio's assets for temporary or emergency purposes.

MCL 129.91 and 129.93

HOUSE COMMITTEE ACTION:

The House Committee on Local Government adopted a substitute that is substantially similar to the Senate-passed version but provides slightly different definitions of "investment officer" and "public corporation"; delays the effective date of the requirement that a local unit adopt an investment policy from 180 days after the bill's effective date to 180 days after the end of the first fiscal year following the bill's effective date; and removes an exemption from the requirement that an investment policy be adopted, which the Senate-passed version contained for local units whose funds are kept only in bank accounts.

FISCAL IMPLICATIONS:

The Senate Fiscal Agency reports that the bill would have no fiscal impact on state government and no measurable impact on local governments. (SFA floor analysis dated 10-16-97)

ARGUMENTS:

For:

The bill would provide a much-needed updating of Public Act 20 of 1943, which regulates how local units of government may invest "surplus" funds. (This does not apply to pension funds.) Its proponents say the bill has three major purposes: to require a written investment policy approved by the public body of a public corporation; to make vendors and brokers of investment products more accountable; and to make the act more like the investment regulations for school districts. Generally, it provides more investment flexibility for local units. It also updates descriptions of authorized investments and clarifies the act by providing new definitions of such terms as "public corporation", "funds", and "investment officer". Many local units already have investment policies; it makes sense for all local units to adopt a policy to guide the investment of public money.

Against:

Is it really the state's job to mandate that local governments adopt investment policies? Local officials, including a majority of treasurers, are themselves elected by the people and are capable of deciding the need for such policies.

Response:

Public Act 20 has for over 50 years contained provisions regulating how local units can invest their surplus funds,

so mandating the adoption of an investment policy is hardly a new departure in state-local relations. Besides, while the bill says local units must have a policy it also provides them with more flexibility for investing than is now the case.

POSITIONS:

The Department of Treasury supports the bill. (12-2-97)

The Michigan Municipal League supports the bill. (12-9-97)

The Michigan Bankers Association has indicated support for the bill. (12-9-97)

The Michigan League of Savings Institutions has indicated support for the bill. (12-9-97)

The Michigan Townships Association has no position on the bill. (12-9-97)

Analyst: C. Couch

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.