Legislative Analysis

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CDARS FOR COMMUNITY COLLEGES INVESTMENTS

Senate Bill 583 as passed by the Senate
Sponsor: Sen. Tony Stamas
House Committee: Banking and Financial Services
Senate Committee: Banking and Financial Institutions

Complete to 8-14-09

A SUMMARY OF SENATE BILL 583 AS REPORTED FROM HOUSE COMMITTEE 6-18-09

The bill would amend the Community College Act of 1966 to increase the investment options available to community colleges. Currently, the act restricts investment of debt retirement funds, building and site funds, building and site sinking funds, and general funds to the district to numerous options specified in the act, such as U.S. bonds negotiable certificates of deposit, savings accounts, or other interest-earning deposit accounts of a financial institution; or mutual funds, trusts, or investment pools composed entirely of instruments that are eligible collateral.

Senate Bill 583 would amend the act (MCL 389.142) to specify that the treasurer of a community college could invest in certificates of deposit (CDs) issued in accordance with the following conditions:

- The funds were initially invested through a financial institution that was not ineligible to be a depository of the state's surplus funds under Section 6 of Public Act 105 of 1855.

- The financial institution arranged for the investment of the funds in CDs in one or more insured depository institutions (i.e., a bank or savings institution whose deposits are insured by the FDIC) or one or more federal credit unions (i.e., a credit union whose member accounts are insured by the National Credit Union Share Insurance Fund) for the account of the community college district.

- The full amount of the principal and any accrued interest of each certificate of deposit was insured by an agency of the U.S.

- The financial institution acted as custodian for the community college district with respect to each certificate of deposit.

- At the same time that the funds of the community college district were deposited and the CDs issued, the financial institution received an amount of deposits from customers of other insured depository institutions or insured credit unions equal to or greater than the amount of the funds initially invested by the community college district through the financial institution.

BACKGROUND INFORMATION:

Public Acts 307 and 308 of 2008 allowed school districts, intermediate school districts, and public corporations to invest funds in certificates of deposit with financial institutions that participate in programs such as the Certificate of Deposit Account Registry Service program, also known as CDARS. Public Acts 21 and 22 of 2009 (enrolled Senate Bill 195 and House Bill 4397) allowed these entities to also invest in certificates of deposit issued by insured credit unions.

The Certificate of Deposit Account Registry Service program, or CDARS, is a funding tool through which financial institutions, such as banks and credit unions, can offer customers insurance on deposits greater than $250,000 (recently increased from the previous cap of $100,000). A person with more than $250,000 to invest must divide the investment between two or more financial institutions in order to have the total amount of principal and accrued interest insured against loss under the FDIC insurance.

CDARS is a network of about 1,600 financial institutions. When Depositor A invests, say, $300,000 in a CD in an institution that is a member of the CDARS network, up to $245,000 is invested in a CD at that institution. The rest (in this scenario, $55,000) is deposited in a CD offered by one or more member institutions. In this way, the depositor's total investment, including accrued interest, will fall below the FDIC's cap of $250,000 and be fully insured. At the same time, an equal amount of funds from the member institution receiving the excess investment (from Depositor B) will be placed in Depositor A's bank. Thus, both Depositor A and B will have their investments exceeding $250,000 fully insured. A complex computer program matches the institutions involved in the transaction.

The benefit to consumers and governmental entities is that larger sums of money can be invested in CDs at a single local bank and be fully insured even though the total investment is more than $100,000. The benefit to smaller community banks is that CDARS attracts and retains otherwise uninsurable funds back to the local bank, thus making more revenue available to offer in loans to community members.

Credit unions currently cannot participate in the CDARS system as their deposits are not insured by the FDIC. Instead, they are insured by the National Credit Union Administration (NCUA), which is also their federal regulator. However, CDARS may become open to participation by credit unions in the future, or a parallel registry could be developed. If so, some feel state law should be changed now so that credit unions could be in position to accept deposits by municipalities and school districts and invest them in these higher yielding instruments.

FISCAL IMPACT:

Senate Bill 583 would have a positive fiscal impact on community colleges by allowing them to increase their investment flexibility and help reduce potential administrative costs of splitting investments among multiple institutions. Moreover, the bill would expand FDIC coverage for community college investments using the certificate of deposit account registry service program.

POSITIONS:

A representative of the Michigan Community College Association testified in support of the bill. (6-18-09)

The Michigan Bankers Association indicated support for the bill. (6-15-09)

The Michigan Credit Union League indicated support for the bill. (6-15-09)

Delta College indicated support for the bill. (6-18-09)

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■ 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.