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BILL ANALYSIS

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Senate Bill 583 (Substitute S-1 as reported) *(as enacted)*
Sponsor: Senator Tony Stamas
Committee: Banking and Financial Institutions

Date Completed: 6-1-09

RATIONALE

Community colleges are subject to certain restrictions when investing funds. Among the permitted investments under the Community College Act is a certificate of deposit at a State or nationally chartered bank or credit union that maintains a principal office or branch office in Michigan. Certificates of deposit offer a virtually risk-free return because they are guaranteed by the Federal Deposit Insurance Corporation up to $250,000. Any amount deposited above that limit (which is scheduled to be reduced to $100,000 on January 1, 2014) could be subject to loss in the event of a bank failure. To mitigate that risk, the treasurer of a community college district may spread the college's funds among several institutions, although that can create difficulties in administering the funds. The requirement to deposit money only in financial institutions with a principal office or branch in Michigan also limits the options available to a community college. To address these issues, it has been suggested that a community college should be permitted to deposit its funds into one financial institution that would then distribute those funds among many institutions to ensure that the entire amount was insured.

CONTENT

The bill would amend the Community College Act to allow the treasurer of a community college district to invest certain funds of the district in certificates of deposit (CDs) with a financial institution if that institution arranged for the funds to be invested in CDs in one or more insured depository institutions, the full amount of the principal and interest of each CD were insured by an agency of the United States, and other conditions were met.

The Act permits a community college district treasurer, with the authorization of the board of trustees, to invest debt retirement funds, building and site funds, building and site sinking funds, or general funds of the district. The investment of those funds is restricted to the following:

-- Bonds, bills, or notes of the United States or obligations of this State.
-- Negotiable certificates of deposit, savings accounts, or other interest-earning deposit accounts of a financial institution.
-- Bankers' acceptances issued by a bank that is a member of the Federal Deposit Insurance Corporation (FDIC).
-- Commercial paper supported by an irrevocable letter of credit issued by a bank that is a member of the FDIC.
-- Commercial paper of corporations rated prime by at least one of the standard rating services.
-- Mutual funds, trusts, or investment pools composed entirely of instruments that are eligible collateral.
-- Repurchase agreements against eligible collateral, whose market value must be maintained during the life of the agreements at levels equal to or greater than the amounts advanced.
-- Investment pools, as authorized by the Surplus Funds Investment Pool Act, composed entirely of instruments that are legal for direct investment by a community college.

The bill also would permit the treasurer of a community college district to invest those funds in certificates of deposit issued in accordance with the following conditions:

-- The funds initially were invested through a financial institution that was not ineligible to be a depository of surplus funds belonging to the State under Section 6 of Public Act 105 of 1855 (described in **BACKGROUND**, below).
-- 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 insured 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.
-- The full amount of the principal and any accrued interest of each CD was insured by an agency of the United States.
-- The financial institution acted as custodian for the community college district with respect to each CD.
-- At the time that the funds were deposited and the CDs were issued, the financial institution received an amount of deposits from customers of other insured depository institutions equal to or greater than the amount of the funds initially invested by the community college district through the financial institution.

MCL 389.142

BACKGROUND

Federal Deposit Insurance Corporation

The FDIC is an independent agency of the Federal government created to insure bank deposits against losses in case of a bank failure. The program is funded through premiums paid by participating financial institutions, and depositors are insured up to a maximum amount. On October 3, 2008, the FDIC increased the maximum insured amount to $250,000 per depositor. The FDIC will reinstate the previous maximum of $100,000 on January 1, 2014.

National Credit Union Administration (NCUA)

The NCUA is an independent agency of the Federal government similar to the FDIC, created to oversee Federal credit unions. It administers the National Credit Union Share Insurance Fund, which guarantees the return of a member's shares up to $250,000. The maximum insured amount will return to $100,000 on January 1, 2014.

Surplus State Funds

Public Act 105 of 1855 governs the deposit of surplus State funds. Under Section 6 of the Act, if a financial institution is found to have engaged in an illegal discriminatory lending practice related to a mortgage loan or home improvement loan application, the Commissioner of Financial and Insurance Regulation may prohibit additional surplus funds belonging to the State from being deposited in that financial institution, based on the nature of the violation, the actions taken to prevent future violations, and the institution's record in complying with laws prohibiting such discriminatory practices.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill would allow community colleges to participate in the Certificate of Deposit Account Registry Service (CDARS), a network of financial institutions created to help large depositors protect their investments against the possibility of bank failure. Under CDARS, when one participating institution receives a large deposit from a client, it spreads that amount among other institutions as necessary to keep the amount at any one institution below the maximum amount insured by the FDIC. In that way, the CDARS network allows the depositor to insure the entire amount of a large deposit without having to keep track of multiple accounts at different institutions, simplifying its accounting and reducing administrative costs.

The recent financial crisis has demonstrated the need for protection against the possibility of bank failures, and the bill would allow community colleges to obtain that protection while meeting the investment restrictions under the Community College Act. The Act requires a community college to invest only in financial institutions that maintain a branch or office within the State. Under the bill, a community college would have indirect access to any financial institution in the CDARS network, as long as the initial deposit was made in a financial institution that met the requirements of the Act.

The bill would not result in any net outflow of bank deposits from the State, however, because each institution that distributed funds under the bill would have to receive an equal amount of deposits from the receiving institution, leaving each bank with the same net deposits.

School districts and municipalities already are permitted to participate in the CDARS network under Public Acts 307 and 308 of 2008, and the bill would allow community colleges to take advantage of the same investment opportunities.

While the CDARS network currently consists of depository institutions only, the bill would include credit unions as well. Thus, if the scope of the program changed, there would be no statutory restriction preventing credit unions from accepting a community college's funds through the network.

Legislative Analyst: Curtis Walker

FISCAL IMPACT

The bill would result in additional FDIC coverage by allowing community college districts to use the Certificate of Deposit Account Registry Service Program as an investment tool.

Fiscal Analyst: Bill Bowerman