Legislative Analysis

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CDARS: ALLOW AS INVESTMENT OPTION FOR SCHOOL DISTRICTS & PUBLIC CORPORATIONS

House Bill 6297
Sponsor: Rep. Ed Clemente

House Bill 6298
Sponsor: Rep. Andy Couloris
Committee: Banking and Financial Services

Complete to 9-15-08

A SUMMARY OF HOUSE BILLS 6297 AND 6298 AS INTRODUCED 6-27-08

The bills would allow school districts, intermediate school districts, and public corporations to invest certain funds in certificates of deposit with financial institutions which participate in programs such as the Certificate of Deposit Account Registry Service program, also known as CDARS. (For more information on CDARS, see Background Information below.)

House Bill 6297 would amend the Revised School Code (MCL 380.622 and 380.1223) to apply to intermediate school districts and school districts.

House Bill 6298 would amend Public Act 20 of 1943 (MCL 129.91), which pertains to the investment of surplus funds of political subdivisions and limits investments to certain instruments and depositories.

Currently, school districts, intermediate school districts, and public corporations have authority to invest certain funds as specified in statute. One lawful investment option is to invest funds in certificates of deposits issued by financial institutions that maintain a principal office or a branch office located in Michigan. (Public corporations are defined in the act to mean a county, city, village, township, port district, drainage district, special assessment district, or metropolitan district of the state, or a board, commission, or other authority or agency created by or under an act of the state legislature.)

The bills would allow these public entities to also invest funds in certificates of deposit in accordance with the following conditions:

- The funds were initially 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. (Section 6 requires the commissioner of the Office of Financial and Insurance Regulation, or OFIR, to make a determination whether additional surplus state funds shall or shall not be deposited in that institution for a period not to exceed two years, in cases involving a financial institution found to have engaged in an illegal discriminatory lending practice relating to a mortgage loan or home improvement loan application.)

- The financial institution arranged for the investment of the funds in certificates of deposit (CDs) in one or more insured depository institutions as defined in the Federal Deposit Insurance Act for the account of the public entity.

- The full amount of the principal and any accrued interest of each CD were insured by an agency of the United States (e.g., the Federal Deposit Insurance Corporation, or FDIC).

- The financial institution acted as custodian for the public entity with respect to each CD.

- At the same time that the funds of the public entity were deposited and the CD 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 public entity through the financial institution.

BACKGROUND INFORMATION:

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 $100,000. Currently, the Federal Deposit Insurance Corporation (FDIC) insures a deposit from a single investor up to $100,000 in a single institution. A person with more than $100,000 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, $150,000 in a CD in an institution that is a member of the CDARS network, up to $95,000 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 $100,000 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 in CDs greater than $100,000 fully insured. A complex computer program matches the institutions to be 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.

FISCAL IMPACT:

House Bill 6297: The bill would have no fiscal impact on the state but would have a positive fiscal impact on school districts and intermediate school districts. Allowing districts to invest in financial institutions participating in CDARS would increase their investment flexibility and avoid the potential administrative costs of having to independently split investments among multiple institutions, while still insuring their total investment through the FDIC.

House Bill 6298: As written, the bill would have no impact on state revenues or expenditures. It could have a positive impact for those local units of government that elect to take advantage of the additional investment opportunities.

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