

Indiana Association of Cities and Towns

Impact of State and Federal Banking Regulations

Discussion Points

- Indiana Legislative Changes
- Federal Legislative Changes
- Economic Factors
- Deposit and Investment Alternatives
- Summary

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Indiana Board For Depositories

The Indiana Board for Depositories was created as an independent body to insure the safekeeping and prompt payment of all public funds deposited in any depository, to the extent they are not covered by insurance of any federal deposit insurance agency, by maintaining and operating in its own name the Public Deposit Insurance Fund, or PDIF.

- Banks paid assessment for many years
- PDIF grew to approximately \$300 million
- Banking crisis created need for another solution to protect public funds
- HEA 1336-2010

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Indiana Board For Depositories

- HEA 1336-2010 – New Rules for Collateralization
 - New rules established procedures for securing public funds maintained in Indiana designated depositories not insured by a federal deposit insurance program, by the pledge and/or delivery of eligible collateral.
 - Use Highline as a means of determining each banks rating.

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Indiana Board For Depositories

Collateralization Matrix

<u>Highline Rating</u>	<u>Rate</u>	<u>Collateral Basis</u>	<u>Pledge or Deliver</u>	<u>Approx. % of Banks Affected</u>
40-99	0%	None	None	65%
20-39	50%	Avg. Bal. Previous Qtr.	Pledge	20%
0-19	100%	Actual Balance	Deliver	15%

- Eligible Collateral includes:
 - United States Treasury securities
 - Federal agency securities
 - Securities of government sponsored enterprises (e.g. Federal Home Loan Bank, Fannie Mae and Freddie Mac)
 - Irrevocable letters of credit issued by a Federal Home Loan Bank

As of May 2011

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Dodd-Frank Act

- Mandates nearly 250 new regulations and 70 studies
- Creates approximately 13 new agencies including the Financial Stability Oversight Council
- Will impose higher capital requirements on the larger financial institutions
- New regulation will ultimately result in higher costs for all banks

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Economic Factors

- Unemployment rate close to 9%
- U.S. households still deleveraging
- Small business not ready to hire
- Housing continues to struggle
- Global unrest

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Deposit and Investment Alternatives

Ten Steps to Investing Public Funds

1. Identify your objectives
2. Develop an investment policy
3. Develop operational systems and procedures
4. Prepare an investment cash budget
5. Analyze current market rates and develop an investment strategy
6. Determine appropriate investments
7. Track investment results
8. Report results
9. Monitor and make changes as necessary
10. Institutionalize the process

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Deposit and Investment Alternatives

Ten Steps to Investing Public Funds

1. Identify your objectives
 - Improve net interest earnings
 - Safety, liquidity and return
 - Consider staffing
 - Accurate budgeting

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Deposit and Investment Alternatives

Ten Steps to Investing Public Funds

2. Develop investment policy
 - Provides framework and should outline factors such as:
 - Eligible investments
 - Definition of risks
 - Management oversight
 - Reporting
 - Authorized financial institutions
 - Maturity parameters

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Ten Steps to Investing Public Funds

3. Develop operational systems and procedures
 - Written procedures are helpful:
 - Help provide consistency
 - Help ensure compliance with public funds laws
 - Describe who is responsible for various duties

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Deposit and Investment Alternatives

Ten Steps to Investing Public Funds

4. Prepare an investment cash budget
 - The goal to determine “core” balances
 - Identify dollars that can be invested longer
 - Funds such as debt service reserve, rainy day, capital, various utility
 - Take advantage of higher interest rates
 - Can help with long range planning

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Ten Steps to Investing Public Funds

5. Analyze current market rates and develop an investment strategy
 - Determine current interest rate environment
 - Contact your local banker/broker/adviser
 - What does the yield curve look like?
 - Are interest rates going up, down or are they stable?
 - How much and how long to invest

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Ten Steps to Investing Public Funds

6. Determine appropriate investments
 - Indiana Code 5-13-9 describes eligible investments
 - Short-term investments can be immediately turned into cash; checking, savings, sweep, money market mutual funds, LGIP and joint investment funds
 - Intermediate investments have maturities of 30 days to two years; CDs, CDARs, treasuries, agencies and municipal securities

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Short-term Investment Alternatives

INDIANA CODE 5-13 Deposit Accounts

- ❑ Focus on the net rate of return from your bank accounts
 - Goal should be to maximize interest and minimize fees
 - Calculate net rate of return
 - Look for reserve requirements, high transaction charges, FDIC assessment fees
 - Insured by FDIC and PDIF or the new collateral requirements

Reserve Requirement – Banks are required by law to have approximately 10% of all their checking accounts held at the Federal Reserve.

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Short-term Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-11

- Local Government Investment Pool
 - This is the Indiana State Treasurer's Trust Indiana Fund
 - Access funds same day
 - Invest in Indiana eligible investments
 - 50% of the fund must be in Indiana bank deposits
 - Can use other investments such as treasuries, agencies and commercial paper
 - No resolution needed

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Short-term Investment Alternatives

INDIANA CODE 36-1-7

- Interlocal Cooperation
 - This section authorizes the State of Indiana, political subdivisions and state agencies to enter into interlocal cooperation agreements for the joint exercise of powers, including the investment of public funds
 - By passing a resolution, the City or Town may become a participant in the HoosierFund, a statewide investment pool
 - Access funds same day
 - Invest in Indiana eligible investments

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Short-term Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-2.5

☐ Money Market Mutual Funds

- Purchased through depositories designated by the state board of finance as depositories for state deposits.
- The portfolio must be limited to direct obligations of the United States or obligations issued by a federal agency, a federal instrumentality or a federal government sponsored enterprise, or repurchase agreements fully collateralized by such obligations.
- Must be rated AAAm by Standard and Poor's or Aaa by Moody's.
- Federated, Fidelity
- Purchased through local bank/broker

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Short-term Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-3

- Repo Sweeps
 - Made with depositories designated by the state board of finance as depositories for state deposits, and involving the purchase and guaranteed resale of any interest-bearing obligations issued or fully insured or guaranteed by the United States, a federal agency, a federal instrumentality or a federal government sponsored enterprise.
 - Dollars sweep into these accounts at the end of every day.

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Intermediate Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-2

- Government Securities
 - Securities backed by the full faith and credit of the United States Treasury or fully guaranteed by the United States and issued by the United States Treasury, a federal agency, a federal instrumentality or a federal government sponsored enterprise.
 - Securities fully guaranteed and issued by a federal agency, a federal instrumentality or a federal government sponsored enterprise.
 - Purchased through local bank/broker
 - U.S. Treasuries and Agencies are all AAA rated

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Intermediate Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-2

- **Municipal Securities**
 - Added in 2010
 - Municipal securities issued by an Indiana local governmental entity, a quasi-governmental entity related to the state, or a unit of government, municipal corporation, or special taxing district in Indiana, if the issuer has not defaulted on any of the issuer's obligations within the twenty (20) years preceding the date of the purchase.
 - Can be purchased through your local bank/broker

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Intermediate Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-4

- Certificates of Deposit and Deposit Accounts
 - The investing officer shall obtain quotes from each designated depository in the political subdivision.
 - In 2010, a section was added allowing the investing officer to place the deposit in the depository quoting the second or third highest rate of interest.

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Intermediate Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-5

- Authorization to Invest in Certificates of Deposit; Quotes from Depositories
 - This can be a valuable alternative if local banks are not interested in bidding on CDs
 - The board may pass a resolution or ordinance which allows the City or Town to use not only local banks, but also Indiana banks outside the political subdivision
 - More banks participating creates competition

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Intermediate Investment Alternatives

INDIANA CODE 5-13-9 Deposit and Investment Powers

Eligible Investments Indiana Code 5-13-9-5.3

- **CDARS or Certificate of Deposit Account Registry Service**
 - Added in 2010
 - This is another safe investment alternative for Cities and Towns
 - The board may pass a resolution or ordinance which allows the City or Town to utilize CDARS as an authorized investment
 - Many banks in Indiana are members of the CDARS network
 - Fully insured by FDIC

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Deposit and Investment Alternatives

Ten Steps to Investing Public Funds

6. Determine appropriate investments cont.
 - Competitively bid your investments
 - Consider passing the investment resolutions to use CDARS and CDs outside your political subdivision
 - Open and account with state investment pools
 - Super savings accounts with local banks
 - Ask your local banker to get you rates on treasuries, agencies and look for Indiana municipal securities

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Ten Steps to Investing Public Funds

7. Track your results

- Compare earnings versus budget expectations
- Compare results versus leaving all dollars in your bank account

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Ten Steps to Investing Public Funds

8. Report results

- Prepare a report once or twice a year so you are ready for any reporting to your local board or the state board of accounts
- This will show you and others the value of a more structured investment program

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Ten Steps to Investing Public Funds

9. Monitor and make changes as necessary
 - Periodic monitoring of cash budget is required
 - Allows for changes in amounts and how far out to invest

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Ten Steps to Investing Public Funds

10. Institutionalize the process

- One of the goals of the program is to develop a structured and formalized system for investing your public funds
- Executing this process year after year will assist you in improving your investment performance and add additional dollars to your budget

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Summary

- Banks will continue to face regulatory challenges at the federal and state level
- Develop an investment and banking program so you can identify opportunities to increase your net interest earnings
- Consider all the safe investment options the public funds code allows
- Consider expanding investment options
 - Expand certificate of deposit bidding
 - TrustIndiana/Hoosier Fund
 - CDARS
 - Treasuries/Agencies
 - Municipal Securities

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