

Date of Hearing: April 13, 2015

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Matthew Dababneh, Chair

AB 283 (Dababneh) – As Introduced February 11, 2015

SUBJECT: Financial affairs

SUMMARY: Makes permanent, provisions of law that expands the authority granted to local agencies to use a private sector deposit placement service to invest up to 30% of surplus funds into deposits other than certificates of deposits (CDs). Specifically, **this bill:**

- 1) Deletes the January 1, 2017 sunset date that allows a local agency to invest up to 30% of surplus funds in deposits other than CDs at a commercial bank, savings bank, savings and loan association, or credit union that uses a private sector entity to assist in the placement of deposits.
- 2) Repeals a code section that prohibits a local agency from investing more than 10% of its surplus funds in any one private sector entity that assists in non-CD deposit placement service, thereby allowing a local agency to invest up to 30% of surplus funds in one private sector entity that provides deposit placement service.

EXISTING LAW:

- 1) Authorizes a local agency, until January 1, 2017, to invest a portion of its surplus funds in deposits at a commercial bank, savings bank, savings and loan association, or credit union that uses a private sector entity that assists in the placement of non-CD deposits, provided that the purchases of deposits, in total, do not exceed 30% of the agency's funds.
(Government Code, Sections 53601.8 & 53635.8)
- 2) Prohibits a local agency from investing more than 10% of its surplus funds in any single non-CD placement service.
- 3) Provides that the following conditions apply for a local agency to invest its surplus funds in deposits:
 - a) The local agency shall choose a nationally or state chartered commercial bank, savings bank, savings and loan association, or credit union in California to invest the funds, which shall be known as the "selected" depository institution;
 - b) The selected depository institution may use a private sector entity to help place local agency deposits with one or more commercial banks, savings banks, savings and loan associations, or credit unions that are located in the United States and within the network used by the private sector entity for this purpose;
 - c) Any private sector entity used by a selected depository institution to help place its local agency deposits shall maintain policies and procedures that require the following:

- i) The full amount of each deposit placed, including interest, shall at all times be insured by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA); and,
 - ii) Every depository institution where funds are placed shall be capitalized at a sufficient level to receive deposits pursuant to FDIC or NCUA.
- d) The selected depository institution shall serve as a custodian for each deposit; and,
- e) At the same time the local agency's funds are deposited, the selected depository institution shall receive an amount of insured deposits from other commercial banks, savings banks, savings and loan associations, or credit unions that, in total, are equal to, or greater than, the full amount of the principal that the local agency initially deposited through the selected depository institution for investment.
- 4) Authorizes a local agency to invest a portion of its surplus funds in CDs at a commercial bank, savings bank, savings and loan association, or credit union that uses a private sector entity that assists in the placement of CDs, provided that the purchases of CDs, in total, do not exceed 30% of the agency's funds.

FISCAL EFFECT: None.

COMMENTS:

Background

The authorization for local agencies to invest surplus funds in CDs was put into place by AB 2011 (Vargas), Chapter 459, Statutes of 2006. Existing law requires local agency funds to either be protected by federal deposit insurance or secured by collateral. Prior to the bill, if a local agency wanted to make a deposit of over \$100,000, the FDIC insurance limit at the time, the bank had to pledge collateral to secure the deposit. This collateralization requirement was a barrier to most small community banks accepting deposits of local agency funds, which were generally in amounts much greater than \$100,000.

AB 2011 (Vargas) allowed local agencies to use a deposit placement service which takes a bank customer's large deposit and breaks it into amounts of less than the \$100,000 FDIC insurance limit. These amounts are then placed in CDs at other banks within its network, ensuring FDIC protection on the customer's full deposit. The other banks then simultaneously send an equal amount of funds back to the original bank, enabling it to have the full amount of the original deposit available for lending or other purposes. SB 1344 (Kehoe), Chapter 112, Statutes of 2010, eliminated the sunset date contained in AB 2011 (Vargas) and permanently authorized local agencies to use a deposit placement service.

(On July 21, 2010, President Barack Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act, which, in part, permanently raises the current standard maximum deposit insurance amount to \$250,000. The standard maximum insurance amount of \$100,000 had been temporarily raised to \$250,000 until December 31, 2013. The FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category.)

When AB 2011 became law, only one national network, the Certificate of Deposit Account Registry Service (CDARS), Promontory Interfinancial Network, LLC, offered a qualifying CD placement service. In 2010, Promontory Interfinancial introduced Insured Cash Sweep (ICS), similar to CDARS, but allows for more liquid types of deposits like money market accounts, in amounts that qualify for FDIC insurance. These cash sweep services utilizing demand deposit and money market accounts are offered by other private sector entities (including Charity Deposits Corporation, Money Market Account Xtra; and Reich and Tang, Demand Deposit Marketplace).

Most recently, AB 279 (Dickinson), Chapter 228, Statutes of 2013, extended a local government's authority to access these types of cash sweep services. AB 279 expanded the types of deposits local agencies can invest surplus funds into, beyond CDs, to include money market or demand deposit accounts. AB 279 also contains several safeguards to require that a private sector deposit placement service adheres to the federal rules governing FDIC pass-through insurance.

Existing law allows, but does not mandate, a local agency to deposit up to 30 % of their overall surplus funds with a depository institution that uses a private sector placement service. These local agency funds may be deposited into a CD or a demand deposit account. Utilization of a placement service allows the depository institution to accept a deposit from a local agency exceeding the FDIC standard insurance limit of \$250,000 (per depositor) while maintaining full insurance coverage over the entirety of the local agency's deposit. Typically, depository institutions utilizing a placement service are community banks operating within the geographical region of the local agency.

Procedurally, the depository institution selected by the local agency (the "selected depository institution") serves as the custodian of the funds and may use a placement service to place deposits in excess of the FDIC insurance limit with other participating depository institutions within the placement service's network. Existing law mandates that the full amount of each deposit must be insured at all times and that every depository institution where funds are placed must be sufficiently capitalized.

Participating depository institutions receiving a portion of the local agency's deposit from the selected depository institution reciprocate to the selected depository institution deposits equal to that placed with the participating depository institution. This process, memorialized in California statute, provides full insurance coverage for the local agency's surplus funds and allows the local agency to identify one depository institution for which they wish to do business. Without this process, a local agency with surplus funds exceeding the FDIC insurance limit would have the obligation to identify multiple depository institutions to participate out their deposit in order to achieve full FDIC insurance coverage.

For CDs, no more than 30 % of the local agency's overall surplus funds may be deposited into a depository institution where a placement service is used relative to the local agency's deposit. However, for demand deposit accounts, existing law limits the deposit of a local agency's overall surplus funds to no more than 10 % of the agency's funds into any one placement service used by a depository institution relative to the local agency's deposit.

Need for the Bill:

The expanded authority granted by AB 279 (Dickinson) contained a January 1, 2017, sunset date and prohibited local agencies from investing more than 10% of the agency's fund to any one private sector entity that assists in deposit placement service. This bill repeals those two provisions, therefore, permanently extending the authority granted in AB 279 to allow local agencies to invest up to 30% of surplus funds into non-CD deposits at depository institutions that use a private sector entity that assists in the placement of deposits. This bill also removes the limitation on investing authority which prohibited local agencies from investing more than 10% of funds to any one private sector entity that assists in deposit placement service. The overall cap of 30% of surplus funds as well as several other safeguards in current law would not be impacted by this bill.

The changes proposed in AB 283 accomplish two goals: aligns the statutory treatment of demand deposit accounts to certificates of deposit relative to the maximum percentage of surplus funds that may be deposited with a depository institution using a placement service so that each deposit product shall not exceed 30 % of the local agency's surplus funds and eliminates the sunset provision on the code sections permitting a local agency's deposit into a demand deposit account with a depository institution using a placement service.

Previous Legislation:

AB 279 (Dickinson, Chapter 228, Statutes of 2013) authorized local agencies, until January 1, 2017, to invest up to 30% of their surplus funds through a private sector deposit placement service, as specified.

SB 1344 (Kehoe, Chapter 112 Statutes of 2010) deleted the sunset date on current law provisions that allow local agencies to invest up to 30% of surplus funds in CDs with a commercial bank, savings bank, or credit union. Additionally, provides that only a local agency with existing legal authority to make investments may invest surplus funds in CDs.

AB 2011(Vargas, Chapter 459, Statutes of 2006) allowed a local agency to invest specified funds into multiple CDs under certain circumstances.

Double Referral:

This measure previously passed out of the Assembly Local Government Committee on Consent.

REGISTERED SUPPORT / OPPOSITION:**Support**

California Bankers Association (Co-Sponsor)
California Independent Bankers (CIB)

Opposition

None on file.

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