

**FINAL REPORT
OF THE
PUBLIC FINANCE
STUDY COMMISSION**



**Indiana Legislative Services Agency
200 W. Washington St., Suite 301
Indianapolis, Indiana 46204-2789**

November, 2000

INDIANA LEGISLATIVE COUNCIL

2000

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Public Finance Study Commission

Membership Roster

Representatives

Peggy Welch, Chairperson
Bloomington

Dennis Kruse
Auburn

Senators

James Merritt
Indianapolis

William Alexa
Valparaiso

Lay Members

Jerry Ault
Wabash

John Baughn
Columbus

Bonnie Summe
Albion

The Honorable Tim Berry
Indianapolis

Janice Beesely
Washington

Greg Jordan
Indianapolis

Kathy Thompson
Brownstown

Staff

John Rowings
Attorney for the Commission

Beverly Holloway
Fiscal Analyst for the Commission

A copy of this report is available on the Internet. Reports, minutes, and notices are organized by committee. This report and other documents for this Committee can be accessed from the General Assembly Homepage at <http://www.state.in.us/legislative/>.

I. STATUTORY DIRECTIVE

The Indiana General Assembly enacted legislation (IC 5-13-9.1) directing the Commission to do the following:

- (1) Review and evaluate relevant public investment statutes.
- (2) Recommend clarification of definitions with respect to statutes concerning public securities.
- (3) Recommend whether a cap is needed for long term investments by the treasurer of state, and if so, the level of the cap.
- (4) Recommend clarification of public investment statutes.
- (5) Investigate investment options for local units of government.
- (6) Before November 15 of each year the commission meets, prepare and submit a report of the commission's findings and recommendations to the governor and the legislative council.
- (7) Review and make recommendations concerning other relevant issues as decided on by the commission.

II. SUMMARY OF WORK PROGRAM

The Commission met one time during the 2000 legislative interim, on August 22, 2000. The Commission discussed the development of the Indiana Institute for Public Funds Management, the implementation of the legislation enacted pursuant to the Commission's recommendations in prior years, and the general state of Indiana's statutes governing the investment of public funds by the state and by local units of government. The Commission determined that no changes in Indiana's public investment statutes are required at this time and made no recommendations or findings of fact.

The minutes of the Commission's meeting are attached as Exhibit A and are also available through the General Assembly's Internet Homepage at <http://www.state.in.us/legislative/>.

EXHIBIT A

Members

Rep. Peggy Welch, Chairperson
Rep. Dennis Kruse
Sen. James Merritt
Sen. William Alexa
Greg Jordan
Kathy Thompson
John Baughn
Jerry Ault
The Honorable Tim Berry
Janice Beesley
Bonnie Summe



PUBLIC FINANCE STUDY COMMISSION

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LSA Staff:

John Rowings, Attorney for the Commission
Beverly Holloway, Fiscal Analyst for the Commission

Authority: IC 5-13-9.1-1

MEETING MINUTES¹

Meeting Date: August 22, 2000
Meeting Time: 1:30 P.M.
Meeting Place: State House, 200 W. Washington St., Room 404
Meeting City: Indianapolis, Indiana
Meeting Number: 1

Members Present: Rep. Peggy Welch, Chairperson; Rep. Dennis Kruse; Sen. James Merritt; Sen. William Alexa; Greg Jordan; Kathy Thompson; John Baughn; Jerry Ault; The Honorable Tim Berry; Bonnie Summe.

Members Absent: Janice Beesley.

Representative Peggy Welch, Chairperson of the Public Finance Study Commission ("the Commission") called the meeting to order at 1:40 p.m. After the members of the Commission introduced themselves, Representative Welch explained that the Commission had not held a meeting for three years and she had scheduled this meeting because she believed that it was time for an update on the status of Indiana's public investment statutes and was particularly interested in testimony concerning the impact of the 1999 legislation authorizing the state and local units of government to invest

¹ Exhibits and other materials referenced in these minutes can be inspected and copied in the Legislative Information Center in Room 230 of the State House in Indianapolis, Indiana. Requests for copies may be mailed to the Legislative Information Center, Legislative Services Agency, 200 West Washington Street, Indianapolis, IN 46204-2789. A fee of \$0.15 per page and mailing costs will be charged for copies. These minutes are also available on the Internet at the General Assembly homepage. The URL address of the General Assembly homepage is <http://www.ai.org/legislative/>. No fee is charged for viewing, downloading, or printing minutes from the Internet.

in AAA-rated money market funds. She added that at the conclusion of testimony the Commission would decide whether it should conduct additional meetings this year.

Representative Welch asked John Rowings, attorney for the Commission, to provide a brief summary of Commission activity and public investment legislation since 1995. See Exhibit A for a copy of the chronology prepared for Commission members by Mr. Rowings.

Representative Welch then introduced Tim Berry, Treasurer of State, who made the following remarks concerning the development of the Indiana Institute for Public Funds Management:²

- ! There is a need for an information and education resource for local government finance officials, who are responsible for the management of over \$5.5 billion in public funds. The Institute is a continuing education program that will serve as a statewide learning center, providing local government finance officials a forum for information and resources to perform their duties more efficiently. The Institute will address three key public policy initiatives: (1) Increasing the skill level of public funds managers, (2) Increasing the security of public funds, and (3) Increasing the investment earnings from public funds.
- ! Treasurer Berry has been working with the Indiana Fiscal Policy Institute as well as a group of local government finance officials and private sector professionals in developing the Institute.
- ! The Institute has obtained private sector sponsorship and will be conducted at no cost to the state general fund.
- ! It is anticipated that the Institute will conduct three to five one-day seminars around the state each year. Preliminary seminar sites for the first year are Columbus, Evansville, Indianapolis, Fort Wayne and Merrillville, with the first meeting anticipated in Indianapolis in early December.

In response to a question from Representative Welch, Treasurer Berry said that the Treasurer's office has just finished its first year of using AAA-rated money market mutual funds pursuant to the authorization granted by the 1999 legislation. He added that the Treasurer's office is using this authority to provide short-term investments with liquidity and safety, and that these investments over the last year had earned about \$1 million more than they would have if invested under restrictions in place under the prior law.

Representative Welch asked Treasurer Berry how well the Commission's prior legislative recommendations have been working in practice, including the authority for the Treasurer of State to invest in securities with a maturity of up to five years. Treasurer Berry stated that due to current market conditions, it is not prudent to invest tax dollars in long-term obligations (those with a term of more than two years) and that he has not done so during his term of office. He added that some such investments made prior to his term of office are lower performers, but this may not always be the case in the future and does not mean that this option should be eliminated.

Commission member and Marion County Treasurer Greg Jordan made the following remarks concerning his findings during discussions with other county treasurers at a recent State Board of Accounts meeting:

² Information concerning the Institute is available through the Treasurer of State's website at www.state.in.us/tos/public_funds_man_%20page.html

- ! Most counties are still not using AAA-rated money market mutual funds, in part because they are still getting a good rate on their repurchase agreements. This was always intended to be an option, so there is no cause for concern.
- ! The counties that are using AAA-rated money market mutual funds reported a return that is 25 to 28 basis points higher than that received from other products.
- ! There may be some local political issues with respect to making such investments, since they require fiscal body approval at the local level.
- ! More local units will probably begin to use this investment vehicle as they learn more about it and become more comfortable with the concept.

Kerry Spradlin, Indiana Bankers Association, noted her organization's opposition to the 1999 legislation permitting investment of public funds in AAA-rated money market mutual funds and said that so far the impact of that legislation has been minimal. As to the upcoming Institute for Public Funds Management, she said that her organization has mixed emotions - while education and training are obviously good goals, this could make more people aware of the AAA-rated option and result in more money leaving the local community and going to investment brokers. Treasurer Berry noted that the 1999 legislation requires purchase of money market mutual funds through Indiana financial institutions, and Ms. Spradlin responded by stating that smaller banks that do not offer such products may still turn to brokerage firms. Representative Kruse asked if there is a ceiling on the amount of public funds that may be invested in AAA-rated money market mutual funds, and Ms. Spradlin explained the mechanics of the statute (see IC 5-13-9-2.5, which provides that such investments may not exceed 50% of the funds held by the officer and available for investment, with an exception for county treasurers as to a period of a few days surrounding each semiannual property tax installment due date).

Joe DeHaven, Community Bankers Association of Indiana, Inc., noted his organization's involvement in the negotiations leading up to enactment of the 1999 legislation and said that it is still too soon to gauge the impact of that legislation. He said that the Institute for Public Funds Management may have an impact on how the AAA-rated money market mutual funds are used in the future, so it would be prudent to see how this develops and wait for more data before tinkering with the law. He added that community banks are generally having a hard time maintaining deposits, primarily because of the stock market, and this is making it more difficult for community banks to provide loans.

Representative Welch asked Treasurer Berry whether there have been any changes in federal laws governing investment of public funds that require corresponding changes in Indiana's statutes. Treasurer Berry said that there have been no such changes at the federal level.

Treasurer Berry asked Mr. DeHaven and Ms. Spradlin about proposals to increase the amount of FDIC deposit insurance from its current level of \$100,000. Mr. DeHaven said that an effort is under way to increase this amount (if adjusted for inflation since the date of its enactment, it would now be about \$200,000) and that although it is not likely to pass this year, there is a chance that it could be enacted next year. He added that another idea being discussed at the federal level is to have FDIC guarantee 100% of public funds, which is attractive to the 46 states that do not have a state insurance fund like Indiana's Public Depository Insurance Fund (PDIF). Ms. Spradlin added that if FDIC does ever insure 100% of public funds, Indiana's banks should have a voice in what happens to Indiana's PDIF.

Representative Welch asked how much money is currently in PDIF. Treasurer

Berry said that the current balance is about \$288 million and that financial institutions have not been required to pay assessments into the fund during any of the last 14 years. Senator Alexa asked where the interest on PDIF is deposited, and Treasurer Berry responded that the interest is paid back into the fund, pursuant to law.

Representative Kruse asked for a definition of the term "repurchase agreement." Treasurer Berry commented that the statutory definition is a good one (see IC 5-13-9-3 for that definition). Commission member Jerry Ault added that a repurchase agreement could be described as an arrangement under which a financial institution agrees to sell an investor an interest in an investment portfolio with an agreement that the financial institution will buy back ("repurchase") that interest the next day (or at some other specified time).

Senator Alexa asked what impact repurchase agreements have on the rate of return on investment of public funds. Treasurer Berry said that Indiana law removes almost all the risk from investments via repurchase agreements since the permissible portfolio for such an investment must be backed by either PDIF or the federal government. Senator Alexa then asked Treasurer Berry whether he believed that Indiana officials need more investment options. Treasurer Berry said that while he does not want to speak for other officials, he does not believe it is desirable to change the current guidelines as to investment of the state general fund and tax revenues.

Diana Cordray, Clerk-Treasurer of the City of Carmel and legislative liaison for the Indiana League of Municipal Clerk Treasurers, said that she had surveyed the members of the League and that most of them have not yet invested in AAA-rated money market mutual funds. She added that the banking community is not yet actively promoting this investment option and that most of the information concerning it is coming from the Treasurer of State's office.

Representative Welch asked Mr. Jordan whether the General Assembly needs to do anything to increase the investment options available to local government. Mr. Jordan said that based on his conversations with other county treasurers, no additional options are needed at this time. Senator Alexa then asked Mr. DeHaven the converse of Representative Welch's question - are there any investment options that are not permitted for governmental units under current law that the banking community would like to be able to sell to them? Mr. DeHaven said he was not aware of any such need.

Mr. Ault said that there are sufficient investment options available in Indiana for government investment officers, but the real issue is the level of expertise among investment officers at the local level. He then discussed some of the specifics of his bank's investment practices, and noted that PDIF and the conservative investment laws in Indiana generate much respect for the Indiana banks within the national banking community.

Treasurer Berry stated that many banks are reluctant to enter into repurchase agreements with the state because of the size of the state's cash flows, so that is one reason why AAA-rated money market mutual funds have been useful to the state. He added that financial institutions are now able to bid for deposits of public funds via the Internet. Each week, the Treasurer of State's office releases public funds for investment in each of the three geographic regions of the state--north, central and south. Financial institutions then submit bids through the Treasurer of State's website and the investments are awarded to the highest bidder.

Representative Welch asked whether there is a problem with respect to computerization in the offices of some county treasurers and clerk-treasurers. Mr. Jordan

said that it is true that many such officials still do not use personal computers to access the Internet or for e-mail. Ms. Cordray added that communities with high assessed values can provide such equipment to their officials, but that in smaller communities the resources necessary to do so just are not available.

Representative Kruse asked for estimate on the annualized rate of return on repurchase agreements. Mr. Ault said that this varies widely right now, but estimated that it is from a low of 5% to a high of 6.5%.

Mr. Jordan asked who made the decision to stop requiring financial institutions to pay assessments into PDIF. Treasurer Berry explained the statutory procedure under which the Board for Depositories meets to consider this issue.

Representative Welch asked the other Commission members if they agreed that it appeared that no state or local officers were recommending any changes in Indiana's public investment statutes. Treasurer Berry stated that he agreed that no changes are needed as to investment options for the state general fund and general tax revenues, but that it may be desirable to look at further clarifications as to investment of the tobacco settlement trust funds as time passes.

Representative Welch said that there was no apparent need for the Commission to meet again this year since no legislative changes are necessary at this time. She stated that today's meeting had been very useful and thanked all the witnesses and Commission members for their participation. The meeting was adjourned at 3:00 p.m.