SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based only on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 1992

SPONSOR: Comprehensive Planning, Local and Military Affairs Committee and Senator Rossin

SUBJECT: Investment of Public Funds

DATE: April 9, 1999 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Bowman	Yeatman	CA	Favorable/CS
2.	Lombardi	Wilson	GO	Favorable
3.			FP	
4.				
5.				

I. Summary:

The committee substitute provides uniform guidelines for investment of public funds by school districts, counties, municipalities and special districts. The bill creates investment policy guidelines for the investment of the assets of retirement plans subject to chapter 112, Florida Statutes.

This bill amends sections 218.415, 112.661, 112.662, 28.33, 159.46, 219.075, 230.23, and 236.24, Florida Statutes.

The bill repeals sections 237.161(5), 125.31, 166.261, and 218.345, Florida Statutes.

II. Present Situation:

Pursuant to ss. 125.31, 166.261, 218.345, 219.075, and 236.24, F.S., counties, cities, special districts, county officers, and district school boards are authorized to invest surplus public funds. The Local Government Surplus Funds Trust Fund serves as one of the available investment options for these types of funds. Other investment options include: obligations backed by the unconditional guarantee of the United States Government; interest-bearing time deposits in banks organized under the state or the United States; obligations of the Federal Farm Credit Banks or Federal Home Loan Mortgage Corporation; and specified types of securities fully collateralized by United States Government obligations.

Under part IV of ch. 218, F.S., the “Investment of Local Government Surplus Funds Act” (the Act), the Local Government Surplus Funds Trust Fund is created to serve as a repository for surplus funds deposited by units of local government. The fund is administered and managed by the State Board of Administration (SBA) in the same manner and subject to the same restrictions as set forth in s. 215.47, F.S. The SBA uses the same statutory authority to invest funds of the Florida Retirement System.

Section 218.415, F.S., requires that investment activity by a unit of local government must be consistent with a written investment plan or policy adopted by the governing body or principal officer for surplus funds. The plan must provide for liquidity, preservation of capital, and diversity and investments must be selected from a preauthorized list of security issues, issuers, and maturities. Alternatively, units of local government without an investment plan are limited to investing in the following:

- The Local Government Surplus Funds Trust Fund, or any intergovernmental investment pool authorized pursuant to the Florida Interlocal Cooperation Act.
- Securities and Exchange Commission registered money market funds with the highest credit quality rating from a nationally recognized rating agency.
- Savings accounts in state-certified qualified public depositories.
- Certificates of deposit in state-certified qualified public depositories.
- Direct obligations of the U.S. Treasury.
- Federal agencies and instrumentalities.[1]

In addition, a unit of local government investment plan or policy must contain certain other elements that include:

- A description of how the portfolio is structured to match liquidity to pay obligations with investment maturities.
- Arrangements for the holding of the assets of the local government.
- A system of internal controls; and
- Requirements for the chief financial officer to report to the governing body of the local government on the performance of the investment portfolio.

The Auditor General conducted a survey of the implementation of s. 218.415, F.S., by local governments, which is described in Report No. 13283, issued on July 16, 1998. Based on the results of the survey, the report concludes that “many local governments have not fully complied with the requirements set forth in s. 218.415. F.S.” With respect to local governments which limit their investment activities to those investment options listed in subsection (15) of s. 218.415, F.S., the report finds that these local governments not only unnecessarily limit their investment options, but also do not benefit from the investment safeguards afforded by a written investment policy.

[1] “Federal agencies and instrumentalities” include all securities issued by agencies of the federal government or corporations created by Congress, e.g., obligations of the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, etc.

However, in its review of local governments with an adopted investment policy, the results of the survey of local governments indicate that not all local governments follow their investment policy. Specifically, the Auditor General's report finds that the internal controls contemplated by s. 218.415(13), F.S., "have not been effectively implemented to promote compliance with s. 218.415, Florida Statutes." For example, the investment plans of 13 percent of the 95 local governments surveyed did not include a system of internal controls and operational procedures and 41 percent of the plans did not require that the controls and procedures be reviewed by independent auditors as part of the local government's financial audit.

Sections 125.31, 219.075, 166.261, 218.345, and 236.24, F.S., which pertain to counties, municipalities, special districts, and school boards, respectively, impose investment requirements on these local governments that are sometimes inconsistent with, or duplicate the requirements of s. 218.415, F.S.

III. Effect of Proposed Changes:

Section 1. Amends s. 218.415, F.S., to modify the requirements for an investment plan to be developed by a unit of local government and changes the list of authorized investments for units of local governments that elect not to adopt a written investment policy.

Investment Policy

- The bill clarifies that all pension funds, including those governed by chs. 175 and 185, Florida Statutes, are not subject to the investment policy in s. 218.415, F.S.
- The bill prohibits investments that have not been preauthorized and listed in the investment policy (for those units of local government who elect to adopt a policy).
- If the investment policy authorizes investments in derivative products, the bill requires officials responsible for making investment decisions to have sufficient expertise to manage them.
- If used, reverse repurchase agreements must be listed in the investment policy and may only be used for purposes of providing liquidity.
- The investment policy requires that investment maturity dates of securities best match cash flow needs and consider market conditions. Those securities deemed as appropriate should then be competitively bid and the most economically advantageous bid must be selected.
- The investment policy must provide for 8 hours of continuing education annually for local government officials responsible for making investment decisions.

Local government units with a written investment plan are authorized to invest surplus funds in the following:

- The Local Government Surplus Funds Trust Fund.
- Securities and Exchange Commission registered money market funds.
- Savings accounts or certificates of deposits in banks and savings and loan associations.
- Direct obligations of the United States Treasury.

- Securities registered under the Investment Company Act of 1940, as amended, under certain conditions.

Local government units without a written investment plan are authorized to invest surplus funds in all of the above except securities registered under the Investment Company Act of 1940.

Securities

The bill includes a set of safekeeping procedures for local governments to follow regarding securities purchased under section 1 and provides that the governing body of the unit of local government may receive bank trust receipts in return for investment of surplus funds in securities. In addition, the section authorizes the governing body of the unit of local government to sell the security at the prevailing market rate and to deposit the proceeds of the sale into the proper account of the unit of local government.

Audits

The bill provides that certified public accountants conducting audits of units of local government pursuant to s. 11.45, F.S., are required to review, as part of the audit, whether the local government has complied with the investment policy requirements of s. 218.415, F.S. The Auditor General is required to notify the Joint Legislative Auditing Committee of any unit of local government that does not comply with the investment policy requirements of s. 218.415, F.S. Any governmental entity not in compliance with the provisions of s. 218.415, F.S., may be subject to the withholding of payment of funds.

Sections 2. Amends s. 112.625, F.S., clarifying that under the definition of "Statement value" assets for which a fair market value is not provided will be excluded from the assets used in determining the annual funding cost of retirement plans; that under the definition of "fiduciary," "board" or "board of trustees" is synonymous; and that "plan sponsor" means the local governmental entity that has established or may establish a local retirement system or plan.

Section 3. Amends s. 112.661, F.S., to define an investment policy for retirement systems governed by ch. 112, F.S. The investment plan must contain many same elements as the investment plans authorized by s. 218.415, F.S. However, the retirement system investment policies must also include the following:

- A description of fiduciary standards, including a requirement that the board comply with fiduciary standards set forth in the Employee Retirement Income Security Act of 1974.
- Investments must be authorized and listed by the investment policy and the investment of assets of any retirement plan or system are subject to the investment limitations and conditions of ss. 215.47(1), (2), (3), (4), (5), (6), (7), (8), (10), and (16), F.S.
- Provisions for liquidity by matching investment maturities with anticipated cash flow requirements.
- For each actuarial valuation, a determination of the total expected annual, short and long term rate of return, and a requirement that the plan be filed with the division of retirement and the plan's sponsor.

- That investment maturity dates of securities best match cash flow needs and consider market conditions. Those securities deemed as appropriate should then be competitively bid and the most economically advantageous bid must be selected; and
- For each actuarial valuation the board must verify the fair-market value of illiquid investments for which there is no recognized market or pricing mechanism.

Section 4. Amends s. 28.33, F.S., to provide that the investment of surplus funds of the clerk of the court must be invested as described in s. 218.415, F.S.

Section 5. Authorizes the investment of bond proceeds and money held for the payment of debt service on bonds to be invested as provided in s. 218.415, F.S.

Section 6. Allows the investment of surplus funds by county officers, including the tax collector, as provided in s. 218.415, F.S.

Sections 7 and 8. Requires investment policies of school boards to comply with the provisions of s. 218.415, F.S. The list of authorized investments for school board surplus funds set forth in s. 236.24(2)(a), F.S. (1998 Supp.), is repealed.

Sections 9 and 10. Repeals certain sections of law that set individual investment policies for specific units of local government including:

- The investment by a school board of accumulated cash assets not required for a current budget year.
- The investment of county surplus funds.
- The investment of municipal surplus funds; and
- The investment of special district surplus funds.

Section 11. Provides an effective date of October 1, 1999.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

The bill affects the investment conduct of units of local governments including counties, municipalities, special districts and school boards. To the extent investment policies improve cash flow management and the quality of the investment decisions, local governments may experience higher rates of return on investment.

However, those units of local government adopting a written investment policy will incur auditing and continuing education expenses in complying with the requirements of s. 218.415, F.S.

VI. Technical Deficiencies:

None.

VII. Related Issues:

Many local governmental entities invest a portion or all pension fund assets in the Local Government Surplus Funds Trust Fund. The Trust Fund is a highly liquid investment vehicle with shortened investment maturities yielding conservatively lower rates of return (3-5 percent). Pension funds deposited in the trust will not likely meet the actuarially assumed investment return rate used as the underlying basis to fund local government pension plans. For example, a pension plan whose actuarial assumption uses an 8 percent rate of return on investment may fall short of its investment objective by three to five percentage points using the trust fund as an investment vehicle. Although the investment choice may seem prudent, liquid, and safe, it illustrates the inappropriate matching of investment maturity selection with return on investment objectives. As a consequence to this action, the actuarially determined contribution rates may not be sufficient to fund the plan and an unfunded actuarial liability could occur.

This bill represents an amendment to the first statutory policy statement made on this subject by the Legislature in 1995 following widespread financial adversity in market experiences with derivative investments. Three principal units of government were affected in Florida: Escambia County, Palm Beach County (Sheriff’s Office) and a local governmental unit in the Satasota/Manatee area.

VIII. Amendments:

None.