

# Report of the Special Committee on Centralized Pooled Collateral and PMIB Modernization to the 2025 Kansas Legislature

**CHAIRPERSON:** Senator Jeff Longbine

**VICE-CHAIRPERSON:** Representative Nick Hoheisel

**OTHER MEMBERS:** Senators Michael Fagg, David Haley, Rick Kloos, and Robert Olson; and Representatives Mike Amyx, Nikki McDonald, Rebecca Schmoe, Adam Turk, and Laura Williams

## **STUDY TOPIC**

The Committee is directed to:

- Study the centralized pooled collateral for public funds and Pooled Money Investment Board (PMIB) linked deposit loan modernization, as well as the potential impacts of this increased investment in Kansas communities. Such study will permit adequate study of proposed legislation, an opportunity to hear from interested parties, and time for the presentation of a pending economic study that will be available in early October.

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# Special Committee on Centralized Pooled Collateral and PMIB Modernization

## REPORT

### Conclusions and Recommendations

The Committee recommended the Legislature consider legislation:

- Creating a centralized collateral pool program;
- Reducing the statutory certificate of deposit program interest rate for the Pooled Money Investment Board;
- Adjusting the statutory rate that banks are required to offer to guarantee the receipt of public fund deposits, specifically considering options of eliminating the rate, fixing the rate at 2.0 percent below the rate offered by the municipal investment pool, or utilizing the municipal investment portfolio rate as the guaranteed rate;
- Clarifying legislative intent that banks and public entities may negotiate interest rates that differ from the statutorily guaranteed rate;
- Creating a process to ensure public entities are abiding by laws related to the deposit of public funds;
- Clarifying the proceeds from the sale of municipal bonds must be treated the same as all other public deposits;
- Prohibiting third-party investment advisors from being eligible to actively invest public funds for which they are advising; and
- Reworking all state linked deposit loan programs to remove outdated restrictions and improve the competitiveness of Kansas programs, including considering programs adopted by neighboring states.

**Proposed Legislation:** Two bills. The Committee recommended two bills be prepared and introduced by the House Committee on Financial Institutions and Pensions. One bill would incorporate revisions to the state's linked deposit loan programs, and the other bill would incorporate all other recommendations by the Committee.

### BACKGROUND

The Special Committee on Centralized Pooled Collateral and PMIB Modernization (Committee) was created by the Legislative Coordinating Council to study centralized pooled collateral of

public funds in Kansas and modernization of the linked deposit loan programs of the Kansas Pooled Money Investment Board (PMIB).

The need for further study of these topics arose during informational briefings of the House

Committee on Financial Institutions and Pensions during the 2024 Session of the Kansas Legislature and coincided with the pending release of an economic impact study of the impacts of increased investment in Kansas banks.

The Committee was composed of 11 members and authorized to meet for 2 days.

### **COMMITTEE ACTIVITIES**

The Committee met at the Statehouse on November 18 and 19, 2024.

#### **Public Funds Investment Economic Impact Study**

A professor at Fort Hays State University presented a report of an economic impact study of the public funds investment policies of the State. The report concluded that allowing local governments to invest funds outside of the state generally leads to fewer local economic development opportunities and reduced tax revenues for state and local governments.

The report followed up and its results aligned with those of similar studies completed in 1966, 1985, 2004, and 2006.

The report noted that, even if out-of-state investments of local public funds yield higher interest rates, the reduced amount of capital stock available at local financial institutions results in reduced availability of credit for local economic activity, leading to lower overall local economic activity, especially when factoring in compounding impacts of locally financed economic growth.

The report did note that, while local investment of funds is generally more beneficial than out-of-state investment, when interest rates of out-of-state investments significantly exceed local interest rates, the interest rate differential may exceed the overall economic benefits of local deposit of public funds. The study found out-of-state investments would need to offer interest rates more than 3.15 percentage points above the rate available in Kansas for the out-of-state investment to provide more revenues to the State and to local governments than an in-state investment.

### **Review of 2024 HB 2840**

A Senior Assistant Revisor from the Office of Revisor of Statutes reviewed HB 2840 from the 2024 Legislative Session. The bill, which died in committee, would have authorized governmental units to utilize a single pooled collateral system to secure deposits of public funds in certain Kansas financial institutions in excess of the amount insured by the Federal Deposit Insurance Corporation, whereas current law generally requires each deposit of public funds to be secured by a separate and distinct pledge of collateral as security.

The bill would have required the State Treasurer to establish procedures for utilizing the centralized pooled collateral system and to designate a qualified firm to serve as the administrator of the program.

#### **Financial Institutions Analysis and Recommendations**

Representatives of the Kansas Bankers Association provided testimony, noting the current policies for public funds investment in Kansas result in less than 1 percent of the State's pooled money investment portfolio being directly invested with Kansas banks and frequently result in substantial outflows of capital from the state. The representatives recommended various policy changes to increase the amount of Kansas public funds deposited in Kansas financial institutions.

Additionally, representatives of two Kansas-based banks spoke before the Committee, indicating that most banks in Kansas currently have a high demand for credit and they expected a robust market for loans to local business and individuals if additional deposits of public funds were made in the state. The representatives noted that banks in the state are highly regulated and are generally in a strong position with relatively few institutions facing challenges.

#### **Nebraska Centralized Pooled Collateral Program**

A representative of the Nebraska Bankers Association presented information on the operation of the centralized pooled collateral program in Nebraska. The Nebraska program is operated by the insurance subsidiary of the

Nebraska Bankers Association and requires the posting of collateral equal to or exceeding 102 percent of the amount of public deposits held by each financial institution.

The Nebraska program has been operational since 2020 and reports no operational or credit risk problems. The representative mentioned that the transition to a new program can require education of both local governments and financial institutions, but noted that several states have now adopted centralized programs and could share resources regarding a transition period.

### **Linked Deposit Programs Overview and Guiding Principles for Kansas Public Deposits**

The State Treasurer and the Executive Director of the PMIB appeared jointly to present information on the guiding principles for the investment of public funds in Kansas and information on the current Kansas linked deposit loan programs.

For the investment of public funds, the State Treasurer indicated that the security of the funds is always the paramount concern in managing public funds. Secondary concerns include the liquidity of the funds and the return on investment of the funds. The state's inflows and outflows in a day are close to each other on an average day, but on some days outflows may exceed inflows or inflows exceed outflows by several hundred million dollars. Accordingly, the State maintains a certain amount of its public funds in "overnight" funds that are available the following day and are secured by statutorily defined collateral.

The Executive Director of the PMIB indicated that a major concern of the state's investment policies is ensuring the State meets its cash flow needs. The state's linked deposit loan programs frequently have time horizons much longer than most of the State's investments.

The State Treasurer indicated the state's linked deposit loan programs are not widely used and the programs likely would need to be revised if the Legislature would like the programs to be more widely utilized.

The Executive Director of the PMIB indicated the Board was not advocating in favor of or in opposition to any specific policies, but generally supported the guiding principles for public funds investment: security, liquidity, and returns, in that order.

The State Treasurer indicated general support for centralized pooled collateral and provided input on policy considerations of other possible recommendations. He indicated all of the policy issues being considered were appropriate questions for the Legislature, and the State Treasurer's Office would work with the Legislature to implement whatever policy changes were desired.

### **CONCLUSIONS AND RECOMMENDATIONS**

The Committee discussed a need to keep local government funds within local communities while maintaining as much free enterprise as possible and not mandating maximum or minimum interest rates to be paid for any deposits.

The Committee discussed a likelihood that Kansas could benefit from modeling its linked deposit loan programs after those offered by neighboring and surrounding states.

The Committee recommended the Legislature consider legislation:

- Creating a centralized collateral pool program;
- Reducing the statutory certificate of deposit program interest rate for the PMIB;
- Adjusting the statutory rate that banks are required to offer to guarantee the receipt of public fund deposits, specifically considering options of eliminating the rate, fixing the rate at 2.0 percent below the rate offered by the municipal investment pool, or utilizing the municipal investment portfolio rate as the guaranteed rate;

- Clarifying legislative intent that banks and public entities may negotiate interest rates that differ from the statutorily guaranteed rate;
- Creating a process to ensure public entities are abiding by laws related to the deposit of public funds;
- Clarifying the proceeds from the sale of municipal bonds must be treated the same as all other public deposits;
- Prohibiting third-party investment advisors from being eligible to actively invest public funds for which they are advising; and
- Reworking all state linked deposit loan programs to remove outdated restrictions and improve the competitiveness of Kansas programs, including considering programs adopted by neighboring states.

The Committee recommended the bills be prepared in conjunction with representatives of the Kansas Bankers Association and be introduced by the House Committee on Financial Institutions and Pensions during the 2025 Session of the Kansas Legislature.