

A COMMISSION REPORT

*Investment of  
Idle Cash Balances  
By State and Local  
Governments*

ADVISORY COMMISSION ON  
INTERGOVERNMENTAL RELATIONS  
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WASHINGTON 25, D.C.

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<sup>1</sup> Membership on the Commission expired Jan. 20, 1961.

<sup>2</sup> Resigned January 1961.

<sup>3</sup> Membership on the Commission expired Jan. 2, 1961.

<sup>4</sup> Replaced by John Anderson, Jr., Governor of Kansas, Jan. 19, 1961.



## *Preface*

The Advisory Commission on Intergovernmental Relations was established by Public Law 86-380, approved September 24, 1959. Sec. 2 of the Act sets forth the following declaration of purpose and specific responsibilities for the Commission:

Sec. 2. Because the complexity of modern life intensifies the need in a federal form of government for the fullest cooperation and coordination of activities between the levels of government, and because population growth and scientific developments portend an increasingly complex society in future years, it is essential that an appropriate agency be established to give continuing attention to intergovernmental problems.

It is intended that the Commission, in the performance of its duties, will—

- (1) bring together representatives of the Federal, State, and local governments for the consideration of common problems;
- (2) provide a forum for discussing the administration and coordination of Federal grant and other programs requiring intergovernmental cooperation;
- (3) give critical attention to the conditions and controls involved in the administration of Federal grant programs;
- (4) make available technical assistance to the executive and legislative branches of the Federal Government in the review of proposed legislation to determine its overall effect on the Federal system;
- (5) encourage discussion and study at an early stage of emerging public problems that are likely to require intergovernmental cooperation;
- (6) recommend, within the framework of the Constitution, the most desirable allocation of governmental functions, responsibilities, and revenues among the several levels of government; and
- (7) recommend methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government and to reduce the burden of compliance for taxpayers.

Pursuant to its statutory responsibilities, the Commission from time to time singles out for study and recommendation particular problems, the amelioration of which would enhance cooperation among the different levels of government and thereby improve the effectiveness of the federal system of government in the United States.

One problem so identified by the Commission relates to the investment of idle cash balances of State and local units of government and to possible changes in the facilities available to these units in utilizing their cash balances for producing additional revenue. In this report the Commission sets forth the essential facts and policy considerations bearing upon this problem, with particular emphasis upon the intergovernmental relationships involved, and respectfully submits these conclusions and recommendations to the legislative and executive bodies of the States, and of the counties, municipalities and other local units of government. A portion of the report is also directed to the Executive branch of the National Government.

This report was adopted at a meeting of the Commission held on January 18, 1961.

FRANK BANE, *Chairman.*

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## I. *Introduction*

State and local governments in the United States are hard pressed to raise the revenues necessary to keep abreast of an ever broadening and intensifying demand for more governmental services arising from an increasing population and the quickening pace of technological change. The division of tax sources between the National Government on the one hand and States and localities on the other is a very important aspect of this situation and will be the subject of future reports of the Advisory Commission on Intergovernmental Relations. In this report, the Commission invites attention to an opportunity, available through the cooperative endeavors of all three levels of government, to increase State and local governments' revenues *without raising State or local taxes and without increasing other nontax charges upon the public.*

Cash balances of State and local funds which are in excess of operating needs can either be put to work drawing interest and thereby producing additional revenue for the State or local government, or they may be allowed to lie idle. If the latter course is followed, a waste of public funds occurs, just as real as an unnecessary or over-priced procurement contract or an uncollected tax obligation. Although considerable improvements have been registered in recent years, the investment of otherwise idle balances constitutes a significant potential revenue source which still is sometimes overlooked completely and is frequently underutilized. It is the purpose of this report to set forth the historical development and current status of State and local law and practice in this matter and to proffer some suggestions for legislative and administrative action designed to accomplish a fuller utilization of this revenue source by State and local governments. A major emphasis of these suggestions will be upon increased State-

local cooperation but will also include possible cooperative action by the U.S. Treasury.

A time lag often occurs between the receipt of cash and its expenditure. These funds may be utilized by investing them between the time they are acquired and the date they are needed for expenditure. If governmental revenue collections were timed to coincide with or slightly precede expenditures, then reduced idle funds would result. Amounts of idle funds could be lessened by adequate fiscal planning, including careful revenue estimates and related expenditure control. However, it is always essential to maintain adequate working capital, and some idle moneys are unavoidable as a result of complex revenue and expenditure operations.

Cash balances in excess of normal needs arise in a number of ways. Tax revenues are received on one or more "penalty dates" during the year and following their receipt funds on hand will naturally exceed the amount needed for immediate expenditure. Bonds may be sold for financing capital construction, and proceeds from their sale may not be needed for expenditure until later in the construction cycle. This report is concerned with the policy and legal aspects of investment possibilities, of a short-term character, of cash balances from regular operations and from the sale of bonds. The report will not deal with the special problems involved in the investment of retirement and pension funds. These funds generally call for long term, higher yield investments as contrasted to the generally short term and lower yield character of investments into which "operating" funds are placed.

Furthermore, this report will not deal with technical investments or accounting procedures. Professional organizations such as the Municipal Finance Officers Association, International City Managers' Association, and others have published technical manuals dealing with treasury management, projections of cash flow and related matters, and these materials have been used to a good advantage by finance officers of local units of government. Rather, the report which follows will be concerned primarily with policy and legal aspects such as the following: (a) Current constitutional and statutory provisions governing the custody and investment of State funds and funds of counties, municipalities,

special districts, and other local units of government; (b) the extent to which constitutional and statutory modifications might enhance the interest revenues of State and local units; (c) necessity of maintaining “compensating balances” to repay banks for financial services rendered to the unit of government; (d) technical assistance by the States to smaller local units of government in investment matters; and (e) possible cooperative efforts between the National Government and the States regarding the investment possibilities of short-term Treasury obligations. It is the hope of the Advisory Commission that this report will contribute to increased revenue of State and local governments and to improved intergovernmental relations in this area.

## II. *Historical Developments Regarding the Custody and Investment of Government Funds*

A drastic change has occurred over the past quarter century in public attitudes and private ethics with respect to the custody and handling of government funds. The late Leonard D. White made the following observation in 1955:

It is impossible to estimate the amount of private gain that has been pocketed by the custodians of public money during the nineteenth and early part of the twentieth century. The sum would certainly be great . . . This aspect of treasury management has now passed into the more staid . . . period of accurate accounting and public control.<sup>1</sup>

A recitation of the many scandals associated with the custody of State and local funds in the United States would expand this report to undue length and would serve no purpose other than to further document the tremendous progress which has been made in this area of public administration. Let it suffice here to summarize the principal developments which have characterized the offices of State and local treasurers and finance officers over the years and the major changes in policy and practice which have occurred, with an occasional example characteristic of the period.

The experience of the National Government in the nineteenth century is of significance because of the effects on State and local practice. It became a duty of the first Bank of the United States (1792-1812), as a condition of its charter and Federal subscription of 20 percent of its capital stock, to receive and have custody of Federal revenue, and to transfer funds from one part

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<sup>1</sup> White, Leonard D., *Introduction to the Study of Public Administration*, 4th Edition, Macmillan Co., New York, 1955, p. 237.



of the country to another. The second Bank of the United States (1816–36) performed the same functions. The task was well done; no public money was misapplied and transfers were regularly and promptly made. The Banks were reimbursed by retaining the interest on government money.

The Government withdrew Federal deposits after 1833 and placed its funds in State banks, taking collateral as security. Bank failures in 1837 caused the Government much embarrassment but relatively small eventual losses. Various substitutes were resorted to in an interim period until the establishment of the independent treasury system in 1846 which, in principle, required government funds to be deposited in subtreasuries located in various cities under the direction of assistant treasurers.<sup>2</sup>

During the vicissitudes of “wild cat” banking a considerable number of the States and territories enacted laws modeled after the national independent treasury system, adopting what was then the safest method of keeping the public money. With the development of confidence in the national and State banking systems the crude practice of piling up the State funds in the treasury vaults slowly gave way to the bank depository method of keeping the public funds. A number of the States clung with considerable persistence to the old system. Even as late as 1902 when the bank depository method had been thoroughly tested by experience, 11 States still operated under the independent treasury or vault system. Under this system not only were large funds kept from circulation, thus injuriously affecting business, but the States were deprived of the considerable financial benefit they might have derived had the funds been on deposit in banks drawing even a nominal rate of interest. The system was

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<sup>2</sup> White, *op. cit.*, pp. 235–36. White adds the following note: “In remote parts of the country, however, the problem of safe custody was unsolved. In 1854 a Treasury agent declared that in the whole Ohio Valley the Government had no building or vault in which to deposit a dollar. He described the situation in Jeffersonville, Ind., just across the Ohio River from Louisville. A room adjoining the bar in the chief tavern in the town was judged to afford the greatest available security. Inside it were wooden boxes holding the silver and an iron safe for the gold. Around the room was a low gallery from which the receiver of public money could throw down upon any intruder stone bottles, of which an ample supply was kept in stock. The agent slept in this room with guns, pistols, and pikes. ‘In this fantastical fortification was kept, for years in succession, hundreds of thousands of dollars of the United States money . . .’”

inconvenient and an actual burden to the States and was constantly the object of bitter criticism.<sup>3</sup>

As the independent treasury system gave way to the bank deposit method a number of new questions arose. Who should decide which banks got the public business? What considerations should govern the choice? What security should be required? Prior to 1934, the question of security of the deposits was very important. Although from 1912 to 1917 the aggregate losses of public funds due to bank failures was only \$26,000 for 47 States, this total by 1923 had climbed to \$2,275,000.<sup>4</sup> State and local funds tied up in defunct banks had reached a total of nearly a half billion dollars by the time of the bank holiday in 1933.

During the period of heavy rural bank failures in the United States (1921-33) the deposits of State and local funds were often viewed as a necessary and desirable underpinning of agricultural banks. In Wisconsin and a number of other States official preference was given to the small country banks which made a business of loaning money to the farmers. In many of these cases, the State and local treasurers were limited in withdrawals which could be made because sudden withdrawals of public funds could in some cases cause the immediate failure of the small bank.

The period 1900-1930 was marked by a large number of major scandals.<sup>5</sup> In addition, endeavors to use State funds as an

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<sup>3</sup> Faust, Martin L., *The Custody of State Funds*, National Institute of Public Administration, New York, 1925, p. 6.

<sup>4</sup> Faust, *op. cit.*, p. 24.

<sup>5</sup> Faust cites the following examples: In 1914, a State treasurer of a Western State pleaded guilty to the embezzlement of State funds and received a penitentiary sentence of 5 to 10 years. In 1917 the Governor of a Southwestern State was impeached and removed from office for misapplying and misappropriating the public funds and violating the banking laws. A bank president testified that on one occasion the Governor had visited the bank during his absence and put in two notes for \$25,000 each against which the cashier did not have the nerve to object. In 1922 the Governor of another Southwestern State submitted to arrest on a charge of accepting a bribe to permit the operation of a bank while it was in an alleged insolvent condition. The Governor had also agreed to the placing of \$150,000 of State funds in the insolvent bank in order that it would be permitted to do business. A legislative investigation revealed considerable graft in the banking department with which the Governor had intimate connection. A Midwestern Governor in 1924 received a penitentiary sentence for having appropriated for his own use the funds of certain departments, writing bogus notes, and otherwise using his official position insidiously among banks in a vain effort to rescue his personal affairs. A New England State treasurer in 1924 attempted suicide. It seems that he had deposited State funds to the amount

instrument of rural banking and credit policy resulted in controversy and financial disaster, due both to the agricultural depression and to combinations of political manipulation and faulty management.<sup>6</sup>

Difficulties encountered by State treasurers during this period were duplicated at the county and city levels. These local officials, being elective officers, were subjected to heavy political pressure to place their deposits in such a way as to promote their own and their party's advantage. All too frequently local treasurers succumbing to this pressure would drift along the path of least resistance, suddenly to find that public responsibility and trust supposed to be theirs had "imperceptibly drifted into the hands of a coterie of irresponsible politicians, who are actuated by ulterior motives, if not by a desire to steal public money."<sup>7</sup>

Gradually at both the State and local levels the practice was discontinued of leaving solely to the treasurer the responsibility for selecting depositories. In State governments it became common to establish depository boards, usually comprising the governor, auditor, attorney general, treasurer, and other elected officials. Likewise in the counties, the county governing boards took over the responsibility for deciding the banks in which county funds should be deposited. Even in these cases however the desire of the local treasurer still carried great weight.

Prior to the inauguration of Federal deposit insurance, security of public deposits was sought by many means. One plan gave preferred status to government deposits in the case of liquidation; another required surety bonds backed by the resources of

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of about \$40,000 in a national bank of which he was cashier, even after the bank was insolvent. He immediately borrowed the money from the bank after having placed it there.

<sup>6</sup> Faust, *op. cit.*, p. 55, points out: For example, in the State of South Dakota a rural credit venture begun in 1917 collapsed completely in 1924, tying up approximately \$2,000,000 of State funds. The rural credit commissioners entrusted with the custody of the fund were largely responsible, since in administering it they had allowed self-interest and thoughts of political power to dominate their duties to the State. Banks in which members of the board were interested carried funds in direct violation of the law. The treasurer of the board used some 107 unauthorized depositories for the deposit of these funds. One bank in which the treasurer of the board had a large interest carried at the time of its collapse rural credit funds to the amount of \$425,000, although under the law it should never have had such funds to the extent of more than \$48,000.

<sup>7</sup> Porter, Kirk H., *State Administration*, F. S. Crofts & Co., N.Y., 1938, p. 106.

surety companies; the most common method was to require collateral security. For a time it seemed that surety bonds might provide a satisfactory means. However, faced with losses of over \$33,000,000 from 1928 to 1933 the surety companies came to regard depository bonds as a highly undesirable class of business.<sup>8</sup> The inauguration of deposit insurance and the stabilization of the banking system subsequent to the banking crash of 1933 has lessened greatly the problem of security of government deposits in commercial banks.

Another historic problem concerned the interest on public funds. A commentary on the extraordinary methods of handling public money is found in the practice, almost universal until about 1900, of allowing treasurers to retain for personal use the interest earned on deposits of public funds. The theory underlying this practice was that the treasurer was responsible only for the safety of the funds committed to him, that the funds were not required nor expected to earn interest, and that any such interest was merely a personal "windfall" of the treasurer. Actually the interest earnings, often very large sums, were widely recognized as the due of the party in power or of the faction to which the treasurer belonged.<sup>9</sup>

By 1920 the doctrine that interest earnings belonged to the State or local treasurer had been generally replaced by the recognition that interest earned on public funds was as truly the property of the government as the funds themselves. Legislation was enacted in a number of States to provide for competitive

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<sup>8</sup> White, *op. cit.*, p. 251.

<sup>9</sup> White, *op. cit.*, p. 237, describes one of the most sensational scandals arising out of private profit from interest earnings, involving an Illinois Governor and former State treasurer. In 1921, the Governor and four other former State treasurers were sued for withholding approximately \$2,500,000 of interest on State deposits. He had placed the State money in an obscure private bank, on which 2 percent was paid. The bank, controlled by an interest ring, then purchased notes of certain large Chicago corporations on which 7 percent interest was earned, thus profiting the insiders by 5 percent. In a civil suit, the Governor was found liable and ordered to make restitution of over \$400,000 of interest earnings wrongfully withheld.

Faust, *op. cit.*, pp. 145-50, cites the following argument of counsel for the Governor's defense: "What am I to do with this money? Am I going down into the State and put \$20,000 in this bank and \$20,000 in that bank, and examine the abstracts of Tom and Bill Jones's land and the affairs of that institution? Why, gentlemen, there would not be vault space enough in the State treasury to take care of the securities for \$8,000,000 deposited in amounts from \$20,000 to \$50,000 through the country banks in the State of Illinois."



bidding by banks in terms of interest rates to be paid on public deposits. Depositories were usually named by the State or locality on a competitive basis, the amounts deposited having a direct relation to the combined capital and surplus of each bank. The contracts were let for fixed periods of time although occasionally indeterminate contracts were entered into which could be annulled by either party upon reasonable notice.<sup>10</sup>

A new problem of interest earnings arose in 1935, when a revision of the Federal banking laws prohibited payment of interest on demand deposits. The practical effect of this rule was to greatly reduce payment of interest on public funds, since both inactive and active treasury balances were often considered as demand deposits. The amounts were very substantial. In 1933 cash on hand and on deposit of the 48 States was over \$3,600,000,000. The interest earnings were obviously great, and after 1935 tended to be taken by the depository banks. Thus in Missouri, it appeared that a balance of about \$90,000,000 to \$100,000,000 of State funds was earning no interest whatever.<sup>11</sup>

However, a number of States and localities began to be increasingly active in authorizing investments in short-term interest bearing obligations of Federal, State, or municipal governments or time deposits in commercial banks. This change marked the beginning of the current period where investment policies of State and local governments are beginning to follow along the general lines of usual business practice. It is remarkable to contemplate that it required a span of one hundred years in the history of American government for prudent and effective treasury management of State and local funds to become the rule rather than the exception.

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<sup>10</sup> Upson, Lent D., *Practice of Municipal Administration*, Century Co., New York, 1926, p. 132.

<sup>11</sup> White, *op. cit.*, p. 237.

### III. Present Situation

#### A. Current Cash and Security Holdings of State and Local Government Funds

In 1959 State and local governments held nearly \$51.3 billion in cash and securities and currently the aggregates are even larger. Detailed data by types of local government are available only for the census year 1957. A general summary of the holdings of State and local governments is shown in table 1.

As shown in table 1, the cash and security holdings of State and local governments in 1957 totaled approximately \$48.5 billion, of which \$30.3 billion was held by State governments and \$18.1 billion by local units of government. Of these total sums, however, a considerable portion consisted of the holdings of insurance trust funds which are maintained separate and apart from other funds to cover the finances of public employe

TABLE 1.—Cash and Security Holdings of State and Local Governments, by Type of Government: 1957

[In millions of dollars]

Item	State and local	States	Local governments					
			Total	Coun- ties	Munic- ipal- ities	Town- ships	School dis- tricts	Special dis- tricts
Total.....	48,483	30,342	18,141	2,573	10,239	494	3,523	1,313
Insurance trust fund holdings, total.....	22,678	17,845	4,832	462	3,825	33	463	110
Unemployment compensation systems.....	8,480	8,422	57	-----	57	-----	-----	-----
Employee-retirement systems.....	12,825	8,050	4,775	462	3,768	33	403	110
Other insurance systems.....	1,373	1,373	-----	-----	-----	-----	-----	-----
Other than insurance trust funds, total.....	25,804	12,496	13,309	2,111	6,413	462	3,120	1,203
By purpose:								
Offsets to debt.....	4,167	1,750	2,417	165	1,721	14	322	195
Bond funds.....	5,374	1,528	3,847	461	1,578	91	1,356	361
All other.....	16,263	9,218	7,045	1,485	3,114	357	1,442	647
By type of holding:								
Cash and deposits.....	11,001	3,913	7,087	1,671	2,580	358	2,037	443
Securities.....	14,804	8,583	6,222	439	3,834	105	1,083	761
Federal.....	10,867	6,176	4,691	400	2,545	84	948	715
State and local.....	2,357	1,190	1,168	20	1,067	4	53	27
Other.....	1,580	1,217	363	19	223	17	84	20

NOTE.—Due to rounding, detail will not necessarily add to totals.

Source: *Census of Governments, 1957*, Bureau of the Census, U.S. Department of Commerce.

retirement systems, the State systems of unemployment compensation, and certain other State-administered insurance systems.

Because of the special characteristics of these various insurance systems, their transactions and assets fall largely outside the scope of the present report. All other financial assets of State and local governments—i.e., exclusive of insurance trust fund holdings—totaled \$25.8 billion in 1957. As indicated by table 1, this included not only assets of what are recognized as ordinary public “operating” funds, but also some \$4.2 billion specifically reserved for future debt retirement and \$5.4 billion of bond fund holdings (borrowing, proceeds, held pending disbursement).

Of this \$25.8 billion held on behalf of noninsurance funds, \$11 billion was in the form of cash and deposits. The remaining \$14.8 billion consisted of \$10.9 billion of Federal securities, \$2.4 billion of State and local government securities, and \$1.6 billion of nongovernmental securities.

For each type of government, table 2 shows the percentage composition of such financial assets by type of holding, together with amounts of interest earnings in fiscal 1957, as reported in the 1957 Census of Governments.

Trend data for years subsequent to 1957 are not available by type of local government. Shown in table 3 are the cash and

TABLE 2.—*Cash and Security Holdings and Interest Earnings of State and Local Governments—Exclusive of Insurance Trust Fund Amounts—by Type of Government: 1957*

Item	State and local	States	Local governments				
			Coun- ties	Munic- ipal- ities	Town- ships	School dis- tricts	Special dis- tricts
Cash and security holdings (exclusive of insurance trust funds):							
Total amount in millions.....	\$25,804	\$12,496	\$2,111	\$6,413	\$462	\$3,120	\$1,203
Percentage distribution:							
Total.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Cash and deposits.....	42.6	31.3	79.2	40.2	77.4	65.3	36.8
Securities.....	57.4	68.7	20.8	59.8	22.7	34.7	63.3
Federal.....	42.1	49.4	18.9	39.7	18.2	30.4	59.4
State and local government.....	9.1	9.5	.9	16.6	.9	1.7	2.2
Other.....	6.1	9.7	.9	3.5	3.7	2.7	1.7
Interest earnings (general revenue, exclusive of insurance trust fund earnings) in millions.....	\$434	\$237	\$26	\$112	\$4	\$33	\$21
Interest earnings as percent of cash and security holdings.....	1.7	1.9	1.2	1.7	.8	1.1	1.7

NOTE.—Holdings data are as of the end of the fiscal year; interest figures pertain to amounts received during the fiscal year. Due to rounding, detail will not necessarily add to totals.

Source: *Census of Governments, 1957*, Bureau of the Census, U.S. Department of Commerce.

TABLE 3.—*Cash and Security Holdings of State and Local Governments—Exclusive of Insurance Trust Fund Holdings: 1955–1959*

[Dollar amounts in millions]

Item	1959	1958	1957	1956	1955
State and local governments, total.....	\$26,741	\$25,881	\$25,804	\$25,387	\$23,725
Cash and deposits.....	11,434	11,520	11,001	11,086	10,689
Securities.....	15,307	14,361	14,804	14,301	13,036
State governments, total.....	\$12,242	\$12,203	\$12,496	\$12,370	\$11,216
Cash and deposits.....	3,780	3,959	3,913	4,036	3,847
Securities.....	8,462	8,244	8,583	8,334	7,369
Local governments, total.....	\$14,499	\$13,678	\$13,309	\$13,016	\$12,509
Cash and deposits.....	7,654	7,561	7,087	7,050	6,842
Securities.....	6,845	6,117	6,222	5,966	5,667
Percent of holdings in cash and deposits:					
State and local governments.....	42.8	44.5	42.6	43.7	45.1
State governments.....	30.9	32.4	31.3	32.6	34.3
Local governments.....	52.8	55.3	53.2	54.2	54.7

NOTE.—Due to rounding detail may not add to totals.

Source: *Governmental Finances in 1959; Governmental Finances in 1958; 1957 Census of Governments*; and for years prior to 1957: *Summary of Governmental Finances*, Bureau of the Census, U.S. Department of Commerce.

security holdings of State governments and local governments combined, for the 5-year period, 1955–59, exclusive of insurance trust fund holdings.

The proportion of State funds held in cash or on deposit declined from 34.3 percent in 1955 to 30.9 percent in 1959, whereas the comparable portion of local funds declined from 54.7 percent in 1955 to 52.8 percent in 1959. The generally downward trend is probably attributable to two principal factors—(a) increasing attention on the part of State and local governments to the investment of idle cash, as discussed later in this section and (b) the increase in interest rates which in turn has motivated the States and local units to minimize their cash balances.

It is interesting to note the wide variation among types of government in the proportion of total holdings represented by “cash and deposits.” This category includes principally: (a) Actual cash; (b) demand deposits with banking institutions; (c) time deposits with banking institutions; and (d) accounts with savings and loan associations. The major bulk of the category is represented by demand deposits. In 1957, the States had 31.3 percent of their non-insurance fund holdings in the “cash and deposits” category. County governments on the other hand had 79.2 percent of their holdings in cash and deposits. It is of course true that other factors being equal, the smaller the number of units of government involved the smaller would be the proportion of cash in relation to total holdings. Further-



more, legal requirements which require the fragmentation of county moneys into many separate funds greatly aggravate the investment problem at the county level. However, the relatively high figure for the counties cannot be explained entirely on these grounds when compared with the figures for municipalities, which had only 40.2 percent of their holdings in cash and deposits.

With respect to securities, States in 1957 had 49.4 percent of their non-insurance fund holdings in Federal securities and 19.2 percent in other securities. Cities had 39.7 percent of their holdings in Federal securities, and 20.5 percent in other securities. Practically all of the security holdings of counties and townships were of the Federal variety.

Of the \$434 million earned as general government revenue during 1957 the States and the cities accounted for \$349 million, with all other units of government accounting for only \$84 million. Both in absolute amount and in relation to total holdings, townships earned the least interest.

Although variations in the distribution of holdings on a national basis among types of government are interesting to note, variations among individual States are even more interesting. Appendix A sets forth the distribution of cash and security holdings by type of holding for each State. (It should be noted that these figures are comprehensive, and include the assets of insurance trust funds, which in many States account for a considerable portion of all the security amounts shown.) Appendix B shows for each State, by type of government, the amount of holdings other than those of insurance trust funds, and the proportion of such holdings in the form of cash and deposits.

It should be emphasized that percentage comparisons drawn from a single year can be misleading because of special circumstances which might have influenced the distribution of holdings at a particular point in time. Furthermore, the data shown in this report reflect conditions as of a given date within a year, when the holdings of particular units might be at an unusually high or low level, depending upon how their revenue collection and budget cycles are structured. Moreover, figures for local governments by type and by State do not, of course, reflect variations among individual units within a given State.

A major proportion of the State and local funds "on deposit" does not bear interest. Table 4 shows the time and demand deposits of State and local governments with insured commercial banks as of June 1959, as reported by the Federal Deposit Insurance Corporation.

TABLE 4.—*Time and Demand Deposits of State and Local Governments With Insured Commercial Banks, June 10, 1959*

[Thousands of dollars]

Size of bank	Deposits of States and subdivisions			Total deposits
	Demand	Time	Total	
Banks with deposits of:				
Less than \$1 million.....	95,690	21,983	117,673	997,546
\$1 to 2 million.....	333,229	71,294	404,523	3,908,630
\$2 to 5 million.....	1,152,086	254,275	1,406,361	14,116,320
\$5 to 10 million.....	1,193,378	308,523	1,501,901	15,972,376
\$10 to 25 million.....	1,373,295	429,015	1,802,310	22,082,883
\$25 to 50 million.....	831,948	321,037	1,152,985	15,730,805
\$50 to 100 million.....	979,864	348,294	1,328,158	15,611,903
\$100 to 250 million.....	1,396,954	403,152	1,800,106	23,355,988
\$250 to 500 million.....	1,257,310	270,271	1,527,581	21,239,160
\$500 to 1 billion.....	673,425	296,748	970,173	19,055,792
\$1 billion or more.....	1,162,107	980,135	2,142,242	54,634,299
Total.....	10,449,286	3,704,727	14,154,013	206,705,702

NOTE.—Statistics of governmental deposits as reported by banking institutions include amounts held for various agency and private trust funds, which are excluded from data on governmental cash and deposits, as reported by the Bureau of the Census.

Source: Federal Deposit Insurance Corporation, *Annual Report*, Dec. 31, 1959.

Federally insured commercial banks are precluded by Federal law from paying interest on demand deposits. Of the approximately \$14.2 billion on deposit by State and local governments \$3.7 billion was on time deposit and \$10.4 billion on demand deposit. State and local deposits for the Nation as a whole made up about 7 percent of total deposits in insured commercial banks as of the date of the report. However, in "small banks" particularly those having less than \$1 million in total deposits, State and local deposits amounted to over 11 percent of total deposits, whereas in the case of the largest banks (\$1 billion or more in deposits) State and local funds accounted for only 4 percent of the total.

Shown in appendix C are time and demand deposits of State and local governments with insured commercial banks by State. In contrast to the national average of 7 percent, in four States, State and local funds make up more than 15 percent of total deposits (Hawaii, Kansas, Mississippi, and New Mexico). The

proportion is the highest in the State of Kansas where, of about \$2.3 billion of total deposits, State and local funds account for \$425 million or 18.7 percent. It will also be noted that in many States the proportion of deposited funds on time deposit (as contrasted to demand deposits) is less than 5 percent. The outstanding exception is California, where 55.4 percent of deposited funds is on time deposit.

### B. *Constitutional and Statutory Provisions Regarding State Funds*

The most recent nationwide study of investment practices of State governments was published in November 1956 by the Public Affairs Research Council of Louisiana.<sup>12</sup> At that time 38 States had varying degrees of authority to invest idle operating funds in securities. Twenty-five of these States and two additional States also utilized time deposits. Therefore as of the end of 1956 a total of 40 States were using some form of investment for idle operating funds, leaving eight States without such a program. These States were Georgia, Indiana, Kansas, Louisiana, Mississippi, Missouri, Nevada, and Oklahoma. Four of the States—Indiana, Kansas, Missouri, and Oklahoma—were specifically precluded from investment. The other four States were not prohibited from investing but lacked permissive legislation. A constitutional amendment permitting investments was approved in the 1956 elections in Missouri,<sup>13</sup> and in 1957 legislation was enacted in Kansas authorizing limited use of time deposits.

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<sup>12</sup> Public Affairs Research Council of Louisiana, *Investment of Idle State Funds*, November 1956.

<sup>13</sup> The influence of constitutional restrictions upon the custody and investment of State funds is illustrated by the sequence of constitutional provisions in Missouri. The constitution of 1875 required that all State funds be placed on demand deposits with banks. However, the State was able to receive interest on these demand deposits until 1933, when, under the provisions of the Federal Reserve Act of 1933 and the regulations of the Federal Deposit Insurance Corporation, insured banks were prohibited from paying interest on demand deposits. The Constitutional Convention of 1944 produced a revised constitution which was adopted in 1945. The new constitution retained the earlier requirement that all moneys in the State treasury should be deposited to the credit of the State in banking institutions.

Specifically, Section 15 of Article IV of the Missouri Constitution of 1945 provided: "The State treasurer shall be custodian of all State funds. All revenue collected and moneys received by the State from any source whatsoever shall go promptly into the State treasury, and all interest, income, and returns therefrom shall belong

In contrast to the rather limited investment of idle operating funds, virtually all States invest idle "nonoperating" funds, including especially funds of State employee retirement systems and other public trust funds. In fact, the rapid growth over the past 20 years of retirement and pension funds for State and local government employees has tended to bring about a liberalization of statutory provisions and administrative practice with respect to the investment of State and local funds generally. Actuarial estimates, upon which retirement funds are based, usually include reasonable estimates for interest earnings; consequently, the necessity and pressure for investment of these funds has been irresistible and a recent survey by the Investment Bankers Association shows that in practically all States a very high proportion of such funds is placed in interest bearing securities.<sup>14</sup>

With respect to operating funds, as of 1956, 12 States were restricted to U.S. Treasury securities in their investments. Eighteen others were authorized to buy their own State issues in addition to Federal securities and a small number of these could also purchase securities offered for sale by political subdivisions within the State.

The treasurers of the various States are generally responsible for fund investment. Where responsibility rests with another agency, the treasurer usually serves as a member of the board, committee, or other agency responsible for the investment

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to the State. Immediately on receipt thereof the State treasurer shall deposit all moneys in the State treasury to the credit of the State in banking institutions selected by him and approved by the Governor and State auditor, and he shall hold them for the benefit of the respective funds to which they belong and disburse them as provided by law. Such institutions shall give security, satisfactory to the Governor, State auditor, and State treasurer, for the safekeeping and payment of the deposits on demand of the State treasurer authorized by warrants of the State auditor. No duty shall be imposed on the State treasurer by law which is not related to the receipt, custody and disbursement of State funds."

In 1945 the attorney general of Missouri interpreted the new provision to preclude the placing of State funds on time deposit at banks. (See Young, George, "Interest on Idle State Funds in Missouri," 1956—unpublished research study on file in Department of Political Science, University of Missouri, Columbia, Mo.) After considerable agitation for change, a constitutional amendment was proposed in 1956 and adopted which provides that all State funds not needed for current operating expenses are to be invested—either in short-term treasury notes or in time deposits at banking institutions.

<sup>14</sup> Investment Bankers Association of America, "State Pension Funds—Digest of Authorized Investments and Actual Investments," Washington, D.C., 1960.

function. At least four States, including Kentucky, Minnesota, New Jersey, and Wisconsin, have organized separate administrative units to conduct the States' entire investment programs, including pension and other nonoperating funds. In 1954 a committee of the National Municipal League developed a "Model Investment of State Funds Law" which was circulated among the States both by the Council of State Governments and by the League. The text of the model law recommended by the League is contained in appendix D.

### *C. State Requirements and Local Practice Regarding Local Funds*

A survey conducted by the Municipal Finance Officers Association in 1953 disclosed wide variation in State laws regarding the investment of idle funds by local units of government. These laws varied from no authority for investment of idle funds in the State of Kansas<sup>15</sup> to rather broad authority in California. In the latter State "sinking funds or surplus money not required for the immediate necessities of a county, city, public district, or any public or municipal corporation may be invested in: (a) bonds issued by the local agency payable solely out of revenues from a revenue-producing property owned, controlled, or operated by it; (b) United States Treasury notes or bonds or those for which the full faith and credit of the United States are pledged for the payment of principal and interest; (c) treasury notes or bonds of the State of California or of any local agency within the State including bonds payable solely out of revenues

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<sup>15</sup> The following observation appeared in the *Topeka State Journal* in November 1958: "Most governmental bodies have a problem with funds which must lie idle until the proper or lawful time comes to check them out. The State of Kansas, by an act of the Legislature, now draws interest on its dormant funds from the banks where they are deposited. The rate of interest (about 1 percent) is low, but at least the funds are no longer completely idle.

"The city also has idle funds, but will have to go to the legislature for authority to invest them. Mayor Schnellbacker has proposed that the city seek such authority.

"Here is a specific illustration of what the city is missing by lacking such authority.

"The Federal Government announced a few days ago that its new issue of 2½ billions of 219-day special treasury bills will yield interest at the rate of 3¼ percent a year. These are generous terms.

"If cities and towns had home rule, they wouldn't have to run to the legislature for permission to increase their revenues in this way."

from a revenue-producing property owned, controlled, or operated by the State or a local agency; (d) registered State warrants. The legislative body can invest only in notes, bonds, or registered warrants which are legal investments for savings banks in California.”<sup>16</sup>

Some States restrict the investment of idle local funds to institutions within the State. Illustrative of this requirement is the North Carolina statute enacted in 1957 which authorized municipalities to invest idle operating funds in (1) certificates of deposit of any bank or trust company having its principal office in North Carolina; (2) a time deposit in any such bank or trust company; and (3) shares of any building and loan association having its principal office in North Carolina but such building and loan deposits cannot exceed the amount insured by the Federal Government. On the other hand, municipalities are authorized to invest capital reserve funds in obligations of the United States or its instrumentalities and obligations of local units of government of North Carolina which have been approved by the Local Government Commission for the purpose of such investment. Capital reserve funds may also be invested in federally insured building or savings and loan associations having their principal office in North Carolina.<sup>17</sup>

While of course local units of government are restricted in their investments of idle funds to the extent set forth in State law, these laws for the most part are permissive rather than mandatory and even where investments are authorized by State law, local units of government may choose not to exercise the authority conveyed by the statute. In a recent survey conducted by the Federal Reserve Board as to the investment of proceeds from the sale of bonds, a number of municipal finance officers indicated that although statutory authority existed for the investment of the proceeds, they felt it was better to keep the money in local banks on demand deposit.

Decisions not to invest idle funds may be taken for a variety of reasons—financial, administrative, or political. Considerable sentiment exists in many localities for “keeping the money at

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<sup>16</sup> Funk, Robert L., “Permissive Legislation Regarding Investment of Governmental Funds,” *Municipal Finance*, February, 1953.

<sup>17</sup> *General Statutes* 159-25; 159.41; 159.42; 160-411.5; and 160-431.

home” rather than sending it to the U.S. Treasury or to the State capital. Illustrative of these decisions was the ordinance adopted by the city of Miami in 1952 (later modified) to “provide that the moneys of the city shall be deposited as demand deposits in all the banks of the city and shall be prorated between said banks upon the ratio that the deposits of each such bank bears to the aggregate deposits of all such banks on the first day of the year.”<sup>18</sup>

A large county in the Washington, D.C. metropolitan area in early 1960 had seven dollars lying idle in open bank deposits for every dollar drawing interest. At the same time neighboring jurisdictions had more than three dollars invested in securities for every two dollars in demand deposits. The county treasurer in explaining which banks received deposits of county funds stated: “You’re in politics, basically; we’ve been trying to keep them all appeased along those lines—it’s a matter of the wheel that squeaks hardest.”<sup>19</sup> On the other hand, examples have been numerous in recent years of aggressive investment practice by local units of government. It has been estimated that Columbia, S.C. is earning an amount in interest about equal to the revenue which would be yielded by a 1¼ mill property tax—due to keeping 90 percent of municipal cash assets in investments. Summit County, Ohio;<sup>20</sup> Milwaukee County; Tacoma; Atlanta; and many other local governments have carried on aggressive investment programs.

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<sup>18</sup> City of Miami, Fla., Ordinance No. 4597.

<sup>19</sup> *Washington Post and Times Herald*, Feb. 7, 1960.

<sup>20</sup> The Summit County experience has been publicized extensively throughout its membership by the National Association of County Officials. From former earnings of \$40,000 annually from a depository contract, 1959 investment income reached over \$200,000. (See pp. 118–121 of proceedings of the *County Finance Congress*, Feb. 14–16, 1960, published by the National Association of County Officials, Washington, D.C.)

## IV. *Policy Considerations*

### A. *Maximization of Revenues*

As stated in the Introduction, it seems fairly clear that interest earnings on cash balances constitute a source of revenue for State and local governments which is frequently under-utilized. Based upon the analyses of current data set forth in the preceding section of this report, it seems evident that the greatest opportunities for increased utilization of this revenue source rests with counties, townships, school, and special districts. However, it is also apparent from the detailed tables in the Appendix that many municipalities and some State governments can improve significantly their revenues in this field. While the Commission would hesitate to put forth anything approaching a firm estimate of the unused potential of this revenue source, a range of \$50 to \$100 million annually does not appear unattainable.<sup>21</sup> This is an order of magnitude which in the view of the Commission warrants the attention of legislative, executive, and financial officials at all levels of State and local government.

It should be noted at this point, however, that the investment of those cash balances which are in excess of operating requirements is only one aspect of the general function of treasury management—the other area of possible major savings being in the reduction of tax anticipation and other temporary borrowing through rescheduling of tax due dates to stabilize the flow of

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<sup>21</sup> For example, on the basis of 1957 local government holdings of \$13.3 billion, if counties, school districts, townships, and special districts had only matched the average practice of municipalities, which had approximately 60 percent of their holdings in securities, an additional \$1.7 billion would have been drawing interest. At 2 percent the interest revenue would have amounted to about \$35 million—or \$50 million at 3 percent. Again, it should be emphasized that census data, reported at a particular point in time, may not accurately reflect the general level of cash and security holdings over an entire year.



revenue receipts.<sup>22</sup> Obviously the reduction of interest costs through a rescheduling of receipts is reciprocal to an increase in interest income through the investment of balances. To the extent that the flow of receipts is stabilized, fewer peaks and valleys appear in the cash picture with a consequent diminution of idle cash needing investment.

An essential procedural aspect to the effective investment of idle cash is the accurate projection of cash flow so that proper maturity dates of investments may be selected. It is not the purpose of this report to get into procedural details; however, since many of the readers are concerned with the entire function of treasury management, there is included in Appendix E for informational purposes a "Procedure for Projecting Cash Flow and Balances" extracted from a general report on treasury management prepared by the League of California Cities.<sup>23</sup>

## *B. Relationships with the Banking Community*

Obviously, the disposition of cash balances of State and local governments is of intimate interest to commercial banks. While State and local funds do not constitute a major segment of total bank deposits (see Appendix C), neither can these funds be termed insignificant. Legislative provisions and administrative polices governing the handling of cash balances must be fair to the banks as well as to the taxpayers at large. On the other hand

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<sup>22</sup> The following statement from the February 1960 Interim Report of the Commission on Governmental Operations of the City of New York, while directed to New York City, is pertinent to large municipalities in general: "The city is under the necessity, quite obviously, of maintaining adequate working cash balances at all times. In months of revenue deficiency, enough short-term borrowing has to be done to keep the cash balance adequate. But in those months in which the inflow of revenue exceeds immediate needs and pushes the cash balance above the level of adequacy, the city is in a position to invest cash temporarily and add to its income. Under an alert cash management policy, the city will not waste money by paying interest on more temporary borrowing than it needs, or by losing interest through failure to invest temporarily any balance in excess of its needs. . . . There are two main ways for the city to reduce net interest cost. One is by better forecasting of cash needs so that borrowing can be minimized. The other is by a series of changes in the revenue collection schedule designed to minimize the month-to-month fluctuations in receipts."

<sup>23</sup> League of California Cities, *Treasury Cash Management and the Investment of Idle Funds*, April 1956.

the governmental units should expect treatment equally favorable to that extended to private customers.

There are two aspects to the size of deposit balances that should be maintained in the depository bank or banks of a governmental unit. One phase, and the easier to determine, relates to the cost of services performed by the bank for the State or municipality. These are somewhat similar to banking services performed for other depositors such as accepting and accounting for deposits, collection services, clearing services, securities custodial services, etc. Also the bank may and often does offer investment and financial advice to the governmental unit, particularly in small towns, cities, and villages. Most banks have established a basis of charges for such services. Using these factors, the State treasurer or local finance officer can determine an approximate minimum balance that probably should be maintained to compensate the bank for services performed. To do otherwise would, in effect, place a financial burden on the bank. A description of procedures sometimes used in arriving at cost factors for banking services, issued by the International City Managers' Association<sup>24</sup> is included for purposes of information as Appendix F to this report.

The second service performed by banks is more elusive to determine but nevertheless must be kept in mind. It relates to the economic functions performed by the banking element. The efficacy with which this function is performed may affect the economic well-being of the municipality. For example, undoubtedly the municipality can benefit from loan activities of a bank. Where loans are made for construction of commercial enterprises or residential properties, the city directly benefits from an increase in taxable values so added. The extent to which the economy is maintained through approximate full employment of the labor force in a local town or city is also a factor since this is reflected, in some degree, in the ability of taxpayers to meet taxes imposed by the municipality. In general, while there is no empiric answer to this question, it should be empha-

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<sup>24</sup> International City Managers' Association, Management Information Service Report No. 170, *Short-Term Investment of Idle Funds*, Chicago, Ill., March 1958. (Copies of this report available only to local governments subscribing to the ICMA Management Information Service.)

sized that the need which existed in the period 1920–33 for the use of State and local funds to protect the solvency of banking institutions is no longer present. Furthermore, the impact of local government deposits or withdrawals is confined largely to the smallest banks in the smallest communities.

### C. *Principles and Types of Investment*

Comment and recommendations to State and local governments as to investment judgments and techniques can come more adequately and appropriately from professional government organizations and from the banking and investment community. Suffice it here to allude to fundamental principles and to summarize the principal types of investment possibilities which are widely utilized by States and localities.

Three primary fundamentals underlie any investment program utilizing public funds:

(a) *Safety*. Regardless of any other considerations the protection of the taxpayers' money is the main objective, and no reasoning to the contrary can justify speculation with the principal amount of the funds to be invested.

(b) *Liquidity*. "When the money is needed it must be available."

(c) *Yield*. If the first two considerations are met, the rate of return becomes a major consideration.

The principal types of investment possibilities may be summarized as follows: (a) U.S. Treasury obligations, including bonds, Treasury bills, and Treasury notes; (b) obligations of the State or of its instrumentalities; (c) obligations of the city, county, or other local unit of government in question; (d) obligations of other States or other local units of government or instrumentalities thereof; (e) obligations of instrumentalities of the United States such as the Federal National Mortgage Association; (f) time deposits in insured banks<sup>25</sup> and (g) interest bear-

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<sup>25</sup> The application of Federal insurance to bank deposits of governmental units has been summarized as follows by the Federal Deposit Insurance Corporation. For insurance purposes, not the public unit, but the officer, employee, or agent who has official custody of the funds and deposits them is the depositor and is entitled to the maximum insurance on such deposits maintained in the same right and capacity. Accounts maintained by him in different rights or capacities are separately insured up

ing accounts with insured savings and loan associations. Additionally, some jurisdictions permit the investment of certain proportions of idle funds in high-grade corporate securities; it should be noted however, that only the larger units of government are likely to have available the technical investment talent to handle transactions of this category. A description of some of the principal types of investment is included, for informational purposes, in Appendix G.

From the point of view of local units of government of small size it can be generally stated that since investment is limited to those choices which provide a combination of stability, liquidity, and minimum fluctuation of principal values, the possibilities frequently narrow down to time deposits and short-term paper of the U.S. Treasury with savings and loan associations and special obligations of housing authorities as additional possibilities where local circumstances permit. It must also be recognized that where the total of funds for investment is very small, the extent of interest return to be gained over and above that available from a time deposit would not compensate for the additional administrative tasks which would be involved in the purchase of bonds.

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to \$10,000 in each right or capacity maintained. Such insurance is separate from the insurance afforded to any other officer, employee, or agent who deposits funds of the same public unit in the same insured bank and separate from the insurance afforded to deposits of his own personal funds. Thus, a county treasurer would be insured up to \$10,000 on his deposits of funds owned by the county, up to \$10,000 on his deposits of funds owned by the State, up to \$10,000 on his deposits of funds owned by an incorporated school district, etc., and up to \$10,000 on deposits of his own funds.

## V. Recommendations

Pursuant to its statutory responsibilities for furthering inter-governmental cooperation, the Advisory Commission on Inter-governmental Relations herewith submits for the consideration of the Governors and legislatures of the several States and the governing bodies and administrative officials of counties, cities, and other local units of government, the following recommendations. These recommendations are designed to further inter-governmental cooperation in order to increase revenues available to State and local units of government. The final recommendation submitted is for the consideration of the Department of the Treasury of the National Government as well as the States and localities.

### A. *Removal of Constitutional and Statutory Prohibitions Against Investment of State and Local Funds.*

*It is recommended that State legislatures take action to remove or initiate the removal of existing constitutional and statutory restrictions upon the investment of the States' own funds and upon the investment by local units of government of funds under their control, at least to the extent of permitting the investment of idle operating funds, as well as balances of other funds not needed for current requirements, in interest bearing deposits with insured institutions and in obligations of the State or of the United States.<sup>28</sup>*

Based upon the facts and considerations set forth in this report, the Commission strongly questions the justification for the con-

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<sup>28</sup> Mayor Celebrezze dissents from this recommendation, believing that the objective would be served more effectively and more directly by amending the Banking Act of 1935 to permit commercial banks to pay interest on demand deposits.

tinuance of State legislative restrictions which preclude the investment, in a safe and prudent manner, by State or local governments of otherwise idle funds. To continue these restrictions upon local governments is not only inconsistent with constructive State-local relations in general, but deprives local units of government of much needed revenue.

The question of how far to go in the type of investments authorized is a matter of judgment which will vary from State to State. At the very least, however, the Commission can see no valid argument against the investment of State or local funds in interest bearing deposits with insured institutions (including, where appropriate, collaterally secured deposits in excess of insurance ceilings), obligations of the U.S. Treasury or those of the State itself. This is not to say that the investment of local funds in the securities of the local unit or in the securities of other States and localities, or in other types of securities would be imprudent if they meet other tests as to liquidity and security.

The Commission suggests that governmental and professional organizations collaborate in the drafting of the following types of model laws for the consideration of State and local legislative officials: (a) A model State law providing for the investment of State funds, including any revisions deemed desirable in the model law for this purpose developed by the National Municipal League and contained in Appendix D of this report; (b) a model State law providing for the investment of idle funds by local units of government; and (c) model local ordinances and charter provisions governing the custody and investment of county, municipal and other local government funds.

## B. *Facilitating Interfund Transfers*

*It is recommended that State and local legislative bodies and administrative officials take action to permit and facilitate temporary transfers among separate funds for purposes of investment and for effective cash management, taking care to ensure that such transfers are of such kind and duration as in no way to impair the credit of the governmental unit concerned.*

Interest earnings on cash balances can often be enhanced through the process of "interfund advances," where such is

legally permitted. Usually, most projections of individual fund cash requirements will show a temporary need at some time during the fiscal year for a loan or an advance from another source. Under proper safeguards, these temporary cash requirements can be met from cash balances in other funds, if legally available for such a purpose. It is important that these advances be guided by certain basic principles, namely (1) the funds can be advanced for the period required; (2) the borrowing fund can repay the advance from estimated revenues when required; (3) the cash advance be repaid as promptly as possible; and (4) the transactions are fully recorded.

### *C. State Technical Assistance to Local Units*

*It is recommended that where such is not already being done, State governments initiate a program of technical assistance to local units of government with respect to the investment of idle funds.*

The Commission firmly subscribes to the general principle that the States have a basic responsibility in assisting and strengthening local government. This responsibility includes the provision by the State to the local units, particularly those of small size, of professional and technical assistance which would be impossible or uneconomical for the local unit to provide for itself.

Many finance officers, particularly in the smaller local units of government, are uncertain as to the interpretation of State laws regarding the investment of idle cash balances, and State governments could perform a highly useful service to these local unit by the issuance of informative and interpretative material. Although local banks provide valuable investment and other financial advice and service to local units of government, the availability of this resource is by no means universal. The interest of the taxpayers of the State and the vitality of local government would be well served by increased leadership and assistance by the States in encouraging and assisting local governments in obtaining increased revenue through interest earnings on invested funds.

#### D. *Publicizing to Local Officials of Regular and Special Offerings of U.S. Treasury Obligations*

*It is recommended that the Department of the Treasury, in cooperation with the investment community and executive and financial officials of States and localities, develop an informational program regarding United States obligations as investment possibilities for State and local funds; this program should include exploring the desirability of special issues of United States securities specially designed to meet the needs of State and local governments.*

As mentioned above, many smaller local units of government are perhaps not aware of all of the investment possibilities extant with respect to interest bearing obligations of the United States, particularly short-term Treasury bills. The Commission believes that the initiation of a cooperative Federal-State informational program, including the preparation of descriptive materials in brochure or other suitable form would be widely helpful. Such materials would constitute a useful element in the program of State professional and technical investment assistance to local units of government recommended above.

The technical problems encountered by State and local governmental units in endeavoring to increase the income on their balances by investment in Treasury issues have been met effectively by many of the larger governmental units which are quite active buyers and sellers of Government securities. Treasury securities are offered in a wide range of maturities and the existence of an active market in these issues provides a mechanism that facilitates such operations. However, there are many governmental units that, either because of their distance from financial centers or the size of their cash balances, feel they are unable to profitably engage in this type of active dealing in Government securities. The costs of informed management and also the dealings in what might be classified as odd lot transactions in a market that is geared to transactions in substantial amounts present certain problems. As a result there have been suggestions that the Treasury provide issues that would be sold exclusively to State and local governmental units in amounts and with maturities that are in keeping with the needs of these units.



# Appendixes



# Appendix A

## Cash and Security Holdings of State and Local Governments, by States: 1957

[Thousands of dollars]

State	Total	Unemployment com- pensation balances— U.S. Treasury	Total exclu- sive of unemploy- ment com- pensation balances	Cash and deposits	Securities				
					Total	Federal	Own gov- ernment	Other State and local	Other
Continental United States.....	48,483,253	8,455,763	40,027,490	11,284,177	28,743,313	17,120,130	3,204,312	2,591,964	5,826,907
Alabama.....	399,145	88,570	310,575	123,643	186,932	94,232	13,288	17,756	61,676
Arizona.....	56,023	209,316	209,316	93,452	115,863	77,579	4,483	29,329	4,372
Arkansas.....	182,971	43,597	139,374	70,444	68,930	44,500	9,455	13,885	1,030
California.....	6,781,202	969,825	5,761,377	1,512,847	4,248,531	2,116,247	38,140	135,555	1,958,589
Colorado.....	430,141	74,560	355,581	118,372	237,209	196,508	6,580	26,981	7,130
Connecticut.....	827,555	246,583	580,972	75,249	505,723	237,807	1,989	96,335	169,782
Delaware.....	85,578	15,507	70,071	36,985	33,086	14,834	1,119	43	18,090
District of Columbia.....	181,820	57,394	124,426	24,361	100,065	100,065			
Florida.....	862,628	93,490	769,138	315,657	453,481	358,370	17,309	68,227	9,575
Georgia.....	687,972	149,747	538,225	248,671	289,554	183,507	11,688	8,629	85,930
Illinois.....	1,087,566	35,947	1,022,809	53,090	979,719	64,494	2,796	11,587	842
Indiana.....	692,917	482,204	643,410	794,195	1,481,427	1,117,881	102,779	169,874	90,893
Iowa.....	541,465	110,289	431,176	375,024	179,812	115,283	2,073	23,964	61,172
Kansas.....	396,003	82,337	313,666	215,081	98,586	84,366	8,267	2,822	3,131
Kentucky.....	376,769	119,960	256,800	120,700	136,111	111,305	1,988	10,483	12,335
Louisiana.....	894,568	142,944	751,629	374,146	377,479	217,101	81,895	55,216	23,267
Maine.....	161,567	45,351	116,016	84,157	81,860	46,023	1,017	137	34,063
Maryland.....	796,947	117,840	679,007	124,819	554,188	443,298	18,734	70,015	22,141
Massachusetts.....	1,227,152	309,938	917,214	317,435	599,779	352,435	33,621	52,224	161,499
Michigan.....	1,764,393	298,945	1,465,448	365,268	1,100,180	854,274	35,154	31,965	178,787
Minnesota.....	695,857	112,296	586,591	195,280	691,301	507,019	40,088	74,869	69,325
Mississippi.....	224,477	33,067	190,810	141,052	46,778	22,243	634	2,621	13,826
Missouri.....	756,463	213,929	567,534	204,088	363,496	258,042		13,079	42,199
Montana.....	198,651	43,839	154,792	69,995	94,797	65,742	1,677	15,730	11,648
Nebraska.....	280,071	37,834	232,217	10,053	142,153	125,822	3,003	4,976	10,162
Nevada.....	65,699	19,940	45,759	16,635	39,161	19,878		15,744	1,386
New Hampshire.....	87,288	23,323	58,963	23,738	35,266	7,416	7	15,744	27,705

*Cash and Security Holdings of State and Local Governments, by States: 1957—Continued*

[Thousands of dollars]

State	Total	Unemploy- ment com- pensation balances— U.S. Treasury	Total exclu- sive of unemploy- ment com- pensation balances	Cash and deposits	Securities				
					Total	Federal	Own gov- ernment	Other State and local	Other
New Jersey.....	1,789,959	441,315	1,348,644	340,634	1,008,010	498,747	32,776	56,887	419,600
New Mexico.....	293,223	38,548	254,675	91,629	163,046	105,870	10,662	41,829	4,685
New York.....	8,470,839	1,271,380	7,199,459	831,151	6,368,308	2,607,237	2,354,908	685,444	720,719
North Carolina.....	801,857	177,242	624,615	150,810	473,805	396,490	441	56,375	20,499
North Dakota.....	223,039	8,890	214,149	118,896	95,252	68,690	1,452	11,722	13,388
Ohio.....	2,854,438	621,190	2,233,248	591,813	1,641,434	1,095,315	44,777	204,916	296,426
Oklahoma.....	466,877	51,925	414,952	187,239	227,713	160,914	34,684	1,296	30,819
Oregon.....	540,815	44,525	496,290	123,536	372,754	256,968	9,414	13,404	92,968
Pennsylvania.....	2,417,438	368,837	2,048,601	412,674	1,635,927	1,072,100	134,637	12,328	416,862
Rhode Island.....	180,424	29,295	151,129	28,000	123,129	99,563	4,935	3,174	15,457
South Carolina.....	281,374	73,236	208,138	70,183	137,953	113,562	13,100	4,896	6,395
South Dakota.....	132,733	13,212	119,521	60,287	59,236	50,663	440	4,028	4,105
Tennessee.....	599,475	90,528	508,947	248,748	260,199	194,463	6,529	25,204	34,003
Texas.....	2,474,730	305,056	2,169,674	822,260	1,347,414	875,234	23,243	296,951	151,986
Utah.....	179,058	38,199	140,859	85,943	54,915	50,373	146	3,072	1,324
Vermont.....	63,435	16,650	46,785	12,425	34,360	9,616	379	230	24,135
Virginia.....	681,784	91,680	590,104	222,432	367,672	225,872	20,178	62,000	59,622
Washington.....	1,128,371	200,381	927,990	166,004	761,987	585,875	52,600	102,037	21,475
West Virginia.....	316,135	65,574	250,561	77,195	173,365	161,476	543	9,782	1,564
Wisconsin.....	1,236,534	252,937	983,597	166,732	816,865	394,534	8,726	28,276	385,329
Wyoming.....	141,569	15,435	126,134	59,588	66,546	42,788	5,220	14,705	3,833
Outside Continental United States (exhibit data):									
Alaska.....	28,227	748	27,479	15,272	12,208	4,905	1,550	-----	5,753
Hawaii.....	202,357	22,604	179,753	58,245	121,508	30,418	341	1,936	88,813
Puerto Rico.....	255,450	-----	255,450	94,642	160,808	104,595	8,126	9,367	38,720

Source: *Census of Governments, 1957*, Bureau of the Census, U.S. Department of Commerce.

# Appendix B

Cash and Security Holdings of State and Local Governments—Exclusive of Insurance Trust Fund Holdings—by States: 1957

State	Amount of holdings (in thousands of dollars)					Percent of holdings represented by cash and deposits				
	State government	Counties	Municipalities	Townships	School and special districts	State government	Counties	Municipalities	Townships	School and special districts
Continental United States.....	12,495,918	2,110,440	6,413,522	461,556	4,323,123	31.3	79.2	40.2	77.4	57.4
Alabama.....	76,947	26,201	74,199	-----	29,191	65.0	63.8	43.3	-----	79.5
Arizona.....	51,749	7,211	14,137	-----	37,987	83.0	83.6	73.2	-----	77.6
Arkansas.....	60,831	8,788	23,409	-----	18,230	51.7	97.8	57.3	-----	84.3
California.....	1,792,133	358,279	643,434	-----	725,785	14.9	89.8	53.9	-----	74.4
Colorado.....	99,768	22,697	54,476	-----	94,743	49.1	70.2	34.6	-----	35.3
Connecticut.....	338,011	1,434	39,823	46,673	11,317	6.5	60.3	44.8	57.1	47.8
Delaware.....	52,074	2,579	7,760	-----	5,985	44.7	100.0	63.6	-----	98.3
District of Columbia.....	-----	-----	93,278	-----	2,157	-----	-----	23.8	-----	91.9
Florida.....	223,065	64,315	213,902	-----	90,974	55.1	65.2	41.3	-----	60.5
Georgia.....	273,432	24,489	62,356	-----	55,819	61.6	77.8	49.5	-----	39.7
Idaho.....	71,033	15,634	7,839	-----	14,419	28.5	97.6	72.4	-----	79.0
Illinois.....	709,724	109,952	376,600	14,231	393,374	46.9	94.6	28.8	99.7	41.2
Indiana.....	277,307	44,419	91,056	3,173	90,487	64.5	92.5	80.3	100.0	81.7
Iowa.....	148,547	51,082	62,343	-----	81,276	61.9	98.7	70.8	-----	75.7
Kansas.....	125,820	40,689	52,808	1,958	65,716	69.6	91.0	77.5	92.0	67.4
Kentucky.....	80,200	16,056	90,525	-----	18,476	76.4	89.4	31.6	-----	85.3
Louisiana.....	315,956	31,037	78,676	-----	105,338	72.6	86.1	63.2	-----	58.9
Maine.....	55,053	1,906	8,091	13,715	4,061	30.7	78.9	54.7	68.2	39.0
Maryland.....	234,601	90,350	69,393	-----	16,947	22.7	53.6	12.1	-----	42.6
Massachusetts.....	203,242	5,134	180,788	132,732	35,893	50.1	98.9	40.6	79.5	39.0
Michigan.....	423,962	50,551	224,937	23,451	275,363	20.1	74.7	43.0	80.5	43.1
Minnesota.....	497,558	40,967	90,670	4,768	91,335	7.7	88.0	54.0	94.7	69.1
Mississippi.....	44,624	32,260	-----	-----	13,192	84.0	85.6	63.3	-----	84.5
Missouri.....	166,820	28,013	139,453	1,003	138,783	57.4	57.2	45.5	100.0	60.9

## Cash and Security Holdings of State and Local Governments—Exclusive of Insurance Trust Fund Holdings—by States: 1957—Continued

State	Amount of holdings (in thousands of dollars)					Percent of holdings represented by cash and deposits				
	State government	Counties	Municipalities	Townships	School and special districts	State government	Counties	Municipalities	Townships	School and special districts
Montana.....	88,787	16,849	10,863	-----	20,570	20.7	90.2	86.4	-----	97.8
Nebraska.....	61,717	30,460	41,407	710	88,534	41.8	82.7	62.2	92.3	34.5
Nevada.....	28,015	7,423	2,347	-----	10,487	81.8	48.4	90.5	-----	73.3
New Hampshire.....	9,159	728	6,570	7,779	4,821	74.1	100.0	55.6	77.5	86.8
New Jersey.....	318,995	51,144	210,282	56,855	126,955	14.5	72.8	65.3	77.8	44.9
New Mexico.....	184,113	8,833	23,668	-----	26,361	28.4	72.8	52.7	-----	75.5
New York.....	1,269,746	159,071	1,503,702	575,293	319,153	15.0	75.4	19.9	94.8	42.0
North Carolina.....	267,836	51,109	66,831	-----	2,737	20.2	87.4	70.5	-----	64.7
North Dakota.....	135,274	12,214	17,881	2,349	19,164	53.8	99.3	68.7	98.9	85.7
Ohio.....	495,525	88,641	421,078	11,556	250,576	37.5	81.7	33.5	96.3	65.8
Oklahoma.....	220,611	18,181	77,575	-----	49,459	40.3	93.0	55.5	-----	72.0
Oregon.....	231,155	39,024	46,928	-----	43,772	17.4	74.1	46.4	-----	69.6
Pennsylvania.....	500,967	110,374	245,553	49,053	230,868	21.2	49.4	41.2	50.3	50.5
Rhode Island.....	35,172	-----	26,055	5,702	1,250	44.5	-----	24.7	49.7	67.0
South Carolina.....	62,435	16,812	19,662	-----	18,650	54.0	53.8	55.2	-----	82.3
South Dakota.....	64,963	17,070	11,883	2,356	20,998	28.3	78.7	77.9	97.2	79.7
Tennessee.....	134,252	62,222	193,605	-----	10,851	93.8	85.0	29.7	-----	65.0
Texas.....	1,061,694	153,489	330,868	-----	251,635	27.9	89.3	63.1	-----	70.0
Utah.....	62,737	5,948	13,375	-----	25,348	85.8	90.0	74.3	-----	61.3
Vermont.....	14,500	45	4,947	8,014	322	18.5	100.0	47.4	82.7	99.4
Virginia.....	303,505	55,784	99,767	-----	12,449	39.6	89.5	46.8	-----	33.8
Washington.....	221,867	34,467	106,630	172	268,294	11.7	69.0	41.1	83.1	22.5
West Virginia.....	58,980	7,006	15,833	-----	12,478	69.0	97.8	73.6	-----	90.0
Wisconsin.....	235,681	72,105	176,874	17,777	78,564	1.7	34.9	32.4	94.3	75.8
Wyoming.....	86,753	5,134	7,125	-----	11,977	39.7	99.0	69.1	-----	78.2

Source: *Census of Governments, 1957*, Bureau of the Census, U.S. Department of Commerce.

# Appendix C

## Demand and Time Deposits of State and Local Governments in Insured Banks by State, Dec. 31, 1959

[Amounts in thousands of dollars]

State	All deposits (public and private)	Time and demand deposits of State and local governments				
		Total		Demand	Time	
		Amount	Percent of all deposits		Amount	Amount
Alabama.....	2,017,465	208,206	10.3	203,119	5,087	2.4
Alaska.....	180,321	19,507	12.2	7,749	11,758	60.3
Arizona.....	1,163,749	131,509	11.3	103,733	27,776	21.1
Arkansas.....	1,246,719	91,621	7.4	89,669	1,952	2.1
California.....	23,822,571	1,818,018	7.6	810,106	1,007,912	55.4
Colorado.....	1,904,715	123,118	6.5	89,556	33,562	27.3
Connecticut.....	2,287,625	102,008	4.5	100,894	1,114	1.1
Delaware.....	600,195	47,273	7.2	34,631	12,642	26.7
District of Columbia <sup>1</sup> .....	1,459,974	140	-----	140	-----	-----
Florida.....	4,728,218	496,787	10.5	397,989	98,798	19.9
Georgia.....	2,819,978	247,278	8.8	232,891	14,387	5.8
Hawaii.....	646,917	112,643	17.4	44,737	67,906	60.3
Idaho.....	645,546	79,218	12.3	79,188	30	.1
Illinois.....	16,839,379	901,049	5.4	697,630	203,419	22.6
Indiana.....	4,597,767	491,351	10.9	431,444	59,937	12.2
Iowa.....	2,984,508	209,351	7.0	203,415	996	.4
Kansas.....	2,274,878	425,277	18.7	366,993	58,344	13.7
Kentucky.....	2,293,532	154,185	6.7	126,414	27,771	18.0
Louisiana.....	2,919,676	432,435	14.8	423,446	8,989	2.1
Maine.....	603,457	31,534	5.2	30,181	1,353	4.3
Maryland.....	2,199,486	147,774	6.7	129,987	17,787	12.0
Massachusetts.....	5,153,360	390,167	7.6	372,165	18,002	4.6
Michigan.....	6,386,170	552,000	6.6	422,911	129,149	23.4
Minnesota.....	4,032,375	269,441	6.7	233,858	30,583	11.4
Mississippi.....	1,327,655	205,200	15.5	204,813	387	.2
Missouri.....	5,953,103	334,137	6.6	343,544	50,593	11.8
Montana.....	805,713	80,658	10.0	68,251	12,407	15.4
Nebraska.....	1,566,392	117,290	7.5	116,051	1,229	1.0
Nevada.....	413,393	33,325	8.1	33,548	24,777	42.5
New Hampshire.....	389,707	28,335	7.3	27,535	800	2.8
New Jersey.....	6,930,023	428,433	6.2	385,337	43,046	10.0
New Mexico.....	694,711	113,142	16.3	83,443	24,699	11.8
New York.....	41,105,098	1,316,008	3.2	1,085,576	230,432	17.5
North Carolina.....	2,763,612	195,405	7.1	159,365	36,040	18.4
North Dakota.....	648,493	29,639	4.6	25,827	3,812	12.9
Ohio.....	11,026,483	717,428	6.5	563,677	153,751	21.4
Oklahoma.....	2,567,039	236,387	9.2	233,663	2,724	1.2
Oregon.....	1,988,410	189,622	9.5	148,606	41,016	27.6
Pennsylvania.....	13,683,959	478,451	3.5	397,374	81,077	16.9
Rhode Island.....	837,224	31,191	3.7	29,584	1,607	5.2
South Carolina.....	1,006,392	117,511	11.7	96,556	20,955	17.8
South Dakota.....	723,949	76,036	10.5	60,439	15,597	20.5
Tennessee.....	3,212,175	242,009	7.5	199,892	42,117	17.4
Texas.....	11,601,074	984,086	8.5	659,190	324,896	33.0
Utah.....	950,611	132,157	13.9	95,616	36,541	17.6
Vermont.....	391,155	17,923	4.6	16,034	1,889	10.5
Virginia.....	3,196,486	242,356	7.6	167,506	74,850	30.9
Washington.....	2,712,258	192,711	7.1	191,595	1,116	1.4
West Virginia.....	1,249,003	100,427	8.0	99,066	1,361	1.6
Wisconsin.....	4,453,624	200,843	4.5	184,080	16,763	8.3
Wyoming.....	405,271	53,074	13.1	44,387	8,687	16.4
Guam, Puerto Rico, and Vir- gin Islands.....	554,946	92,474	16.7	64,046	28,428	30.7
Total.....	219,011,505	14,553,238	6.6	11,432,447	3,120,791	21.4

<sup>1</sup> Deposits of State and local governments exclude those of the District of Columbia, which are included with Federal Government deposits not shown here separately.

Source: Federal Deposit Insurance Corporation, *Report No. 52, "Assets, Liabilities, and Capital Accounts—Commercial and Mutual Savings Banks, Dec. 31, 1959."*

## *Appendix D*

### MODEL INVESTMENT OF STATE FUNDS LAW

AN ACT relating to the establishing and concerning a State Investment Council and a Division of Investment within the State Department of Finance; the centralization of the investment function; and prescribing the classes of securities and other assets in which state funds may be invested.

Be it enacted . . .

#### ARTICLE I.—*State Investment Council*

##### *Establishment*

1. There is hereby established in the State department of finance a State investment council.

##### *Membership*

2. The State investment council shall consist of six voting members: three public members appointed by the governor, two representatives of State funds which own the largest total investment assets, and the State treasurer who shall, however, vote only in case of a tie. The State investment officer shall be a nonvoting member of the council. Actions shall be by majority.

##### *Term of appointments*

3. Each of the public members of the council shall be appointed by the governor for a term of 5 years; except that for the first appointments the terms shall be for 3, 4, and 5 years, respectively. The governor shall also appoint the State fund representatives, but from the membership of the fund governing bodies, and for a term of 5 years, except that the first terms shall be for 1 and 2 years, respectively. All members shall serve until their respective successors are appointed and have qualified.

##### *Qualifications*

4. The public members of the council shall be qualified by training and experience in the field of investment or finance. During his tenure, a mem-



ber of the council or his firm shall not be engaged in the sale of securities to the state or to any fund thereof; nor shall any such member benefit directly or indirectly from any transaction made by the State investment officer; nor shall he hold any office, position, or employment in any political party.

*Removal; vacancy*

5. A public or fund member of the council may be removed from office by the governor, for cause, upon notice and opportunity to be heard at a public hearing. Any vacancy in the membership of the council occurring other than by expiration of term shall be filled in the same manner as the original appointment, but for the unexpired term only.

*Chairman*

6. The chairman and presiding officer of the council shall be the State treasurer.

*Necessary expenses*

7. The members of the council shall serve without compensation but shall be reimbursed for necessary expenses incurred in the performance of their duties as approved by the council.

ARTICLE II.—*Division of Investment: State Investment Officer*

*Establishment*

1. There is hereby established in the State department of finance a division of investment, which shall be under the immediate supervision and direction of a person who shall be designated the "State investment officer."

*State investment officer*

2. The State investment officer shall devote his entire time and attention to the duties of his office, shall not be engaged in any other occupation or profession, nor shall he hold any other public office, appointive or elective. He shall be a person qualified, by training and investment experience, to direct the work of such division. He shall receive a salary of not less than \_\_\_\_\_ thousand dollars (\$ \_\_\_\_\_) annually.

### *Appointment*

3. The State investment officer shall be appointed by the State director of finance with the approval of the governor. Recommendations as to appointments shall be made to the director of finance and to the governor by the investment council together with the detailed qualifications of each person recommended. If within sixty (60) days after the effective date of this act, or after any vacancy, an appointment has not been made, the power of appointment shall vest in the council.

### *Term; removal from office*

4. The investment officer so appointed shall serve without term but may be removed from office for cause, upon notice and opportunity to be heard at a public hearing: (a) by the State director of finance; or (b) by the governor, if a majority of the investment council recommends his removal.

### *Bonding for protection to State*

5. Before the State investment officer, or other responsible employee of the division of investment shall enter upon his duties, the State director of finance shall require an individual bond, or shall include him under a blanket bond, for such an amount and for such coverage as deemed best to protect the State's interest. The premium thereon shall not be chargeable to such officer or employee.

### *Staff and budget*

6. The State investment officer shall annually prepare a budget which shall be reviewed by the council; and, subject to civil service regulations of the State, shall appoint all employees of the division.

## ARTICLE III.—*Centralization of the Investment Function*

### *Transfer of investment powers, functions, and duties*

1. The functions, powers, and duties vested by law in the following enumerated agencies: (list such agencies) relating to investment or reinvestment of moneys and purchase, sale, or exchange of any investments or securities of or for any funds or accounts under the control and management of such agencies, are hereby transferred to and shall be exercised and performed for such agencies by the State investment officer under the supervision of the State director of finance as herein provided.

### *Ex-officio memberships*

2. From and after the effective date of this act, any provision of existing law requiring or designating the State director of finance or the State treasurer to serve, by virtue of his State office, as a member of any of the respective agencies enumerated in Sec. 1 of this Article shall be and become inoperative, and the ex-officio membership in such agencies shall thereupon terminate.

### *Boards, commissions, and fund trustees to continue*

3. Except as otherwise provided in this act:

(1) Each of the respective agencies enumerated in Sec. 1 of this Article shall continue to have all of the powers and shall exercise all the functions and duties vested in, or imposed upon, it by law;

(2) This act shall not affect the terms of office of the present members of such agencies;

(3) Such agencies shall continue to be constituted as provided by existing law; and

(4) This act shall not operate to limit or restrict the members of any such agency, remaining after application of the provisions of Sec. 2 of this Article, from exercising or performing the functions, powers and duties of such agency.

## ARTICLE IV.—*Investment Powers and Duties*

### *Powers and duties of investment officer*

1. Subject to any limitations, conditions, and restrictions contained in policymaking resolutions or regulations approved by the State director of finance, the State investment officer shall have the power to make purchases, sales, exchanges, investments, and reinvestments, for or on behalf of any of the funds or accounts referred to herein; and it shall be his duty to see that moneys invested under the provisions of this act are at all times handled to the best interests of the State.

### *Sales or exchanges of investments*

2. Securities or investments purchased or held under the provisions of this act may be sold or exchanged for other securities or investments; *Provided, however,* That no sale or exchange shall be at a price less than the market price of the securities or investments to be sold or exchanged.

### *Legal opinions*

3. In the purchase of bonds with which approving legal opinions ordinarily are furnished, the State investment officer may require an original or certified copy of the written opinion of a reputable bond attorney or attorneys, or the written opinion of the attorney general, certifying to the legality of such bonds.

### *Powers and duties of investment council*

4. The State investment council shall formulate and recommend to the State director of finance for his approval any investment policy regulations or resolutions pertaining to the kind or nature of investment of any of the moneys, and any limitations, conditions, or restrictions upon the methods, practices, or procedures for investment, reinvestment, purchase, sale, or exchange transactions which, in the majority opinion of the council, should govern the State investment officer.

### *Same; consultation and post review*

5. The council shall meet at least once each month to consult with the State investment officer with respect to the work of the division, and, when required, with the State director of finance. It shall have access to all files and records of the division and may require any officer or employee therein to provide such information as it may deem necessary in the performance of its functions. The council shall inspect and review the respective accounts and funds administered through the division.

### *Defaults; power to compromise*

6. In the event of default in the payment of principal of, or interest on, any investments made, the State treasurer is authorized to institute the proper proceedings to collect such matured principal or interest, and may, with the approval of the State director of finance, after consultation with the investment council, accept for exchange purposes refunding bonds or other evidence of indebtedness at interest rates to be agreed upon with the obligor.

The State treasurer, with the approval of the State's director of finance, after consultation with the investment council, is further authorized to make such compromises, adjustments, or disposition of the past-due interest or principal as are in default, or to make such compromises or adjustments as to future payments of interest or principal as deemed advisable for the purpose of protecting the funds invested; and such adjustments or compromises made and approved are hereby ratified and confirmed.

ARTICLE V.—*Eligibility of Securities and Other Assets for Investment*

*Classes of securities and investments*

1. Moneys made available for investment for a period in excess of one year may be invested in the following classes of securities and investments, and not otherwise:

(1) Bonds, notes, or other obligations of the United States, or those guaranteed by, or for which the credit of the United States is pledged for the payment of the principal and interest or dividends thereof;

(2) Bonds or other evidences of indebtedness of this State; and full faith and credit obligations of, or obligations unconditionally guaranteed as to principal and interest by any other State of the United States, the Territories of Hawaii and of Alaska, and the Commonwealth of Puerto Rico;

(3) Bonds, debentures, notes, or other full faith and credit obligations issued, guaranteed, or assumed as to both principal and interest by the government of the Dominion of Canada, or by any province of Canada; *Provided*, That the principal and interest thereof shall be payable in United States funds, either unconditionally or at the option of the holder;

(4) Bonds, notes, or obligations of any municipal or political subdivision of this State, issued pursuant to a law of this State; *Provided*, That the issuer has not, within ten years prior to the making of the investment, been in default for more than three months in the payment of any part of the principal or interest on any debt evidenced by its bonds, notes, or obligations; and *Provided further*, If the bonds are city or county utility, or utility-district revenue bonds, the revenues of such utility, other than for payment of operation and maintenance expenses, are pledged wholly to the payment of the interest on and principal of such indebtedness, and the utility project has been completely self-supporting for a period of 5 years next preceding the date of investment;

(5) Bonds, notes, or other obligations issued, guaranteed, or assumed by any municipal or political subdivision of any other State of the United States; *Provided*, (a) that any such municipal or political subdivision, or the total of its component parts, shall have a population as shown by the last preceding federal census of not less than 10,000, and (b) the issuer, guarantor, or assumer of such bonds, notes, or other obligations: (i) shall have pledged its faith and credit for the payment of the principal and interest of such bonds, notes, or other obligations; (ii) shall have the power to levy taxes on the taxable real property therein for the payment of both principal and interest of such bonds, notes, or other obligations without limitation of rate or amount; (iii) shall not within 10 years prior to the making of the investment have defaulted in payment of principal or interest of any debt evidenced by its bonds, notes, or other obligations for more than 90 days;

(6) Bonds, debentures, notes, or other obligations issued, guaranteed, or assumed as to both principal and interest by any city of Canada which has

a population of not less than 100,000 inhabitants; *Provided*, That the principal and interest thereof shall be payable in United States funds, either unconditionally or at the option of the holder; and *Provided further*, That all the conditions as prescribed in subsection (5b) of this Article have likewise been met;

(7) Bonds, notes, or other obligations issued, assumed, or unconditionally guaranteed by the International Bank for Reconstruction and Development;

(8) Bonds, debentures, or other obligations issued by a Federal land bank, or by a Federal intermediate credit bank, under the Act of Congress of July 17, 1916, known as the "Federal Farm Loan Act," as amended or supplemented from time to time;

(9) Bonds, debentures, or other obligations issued by any national mortgage association under the Act of Congress of June 27, 1934, known as the "National Housing Act," as amended or supplemented from time to time;

(10) Bonds, notes, or other obligations issued, amended, or unconditionally guaranteed by The Port of New York Authority;

(11) Obligations of any public housing authority or urban redevelopment authority issued pursuant to the laws of this State relating to the creation or operation of a public housing or urban redevelopment authority;

(12) Obligations of any State or municipal authority issued pursuant to the laws of this State; *Provided*, That for each of the five years next preceding the date of investment the income of such authority available for fixed charges shall have been not less than  $1\frac{1}{5}$  times its average annual fixed charges requirements over the life of such obligations;

(13) First mortgages on unencumbered real property when such mortgages are guaranteed or insured in the amount of fifty (50) percent or more of the loan made, in the event of default, by the United States or any agency of the United States Government;

(14) Bonds, notes, debentures, car-trust certificates, preferred stock, or common stock of any corporation organized and operating within the United States; *Provided*, That it shall have minimum assets of ten million dollars (\$10 million) and securities listed on one or more national stock exchanges; *Provided further*, That the combined funds of the State shall not at any one time own more than ten (10) percent of the voting stock of any such company; and *Provided further*, That in the investment of the moneys of any one State fund or account, not more than twenty-five (25) percent of the total of such fund or account shall at any time be invested in the securities of this class (subsection);

(15) Other investments hereafter from time to time authorized by law as legal for investment by insurance companies of this State.

#### *Investment for short-term periods*

2. All surplus cash certified by the State treasurer for short-term investment (1 year or less), or other moneys the principal of which shall be required

within a 12-month period, may be invested in the following classes of securities, and not otherwise:

(1) Certificates or other obligations of the United States, or for which the full faith and credit of the United States is pledged, which mature on such dates as will make available such amount of cash as required;

(2) Any certificates or other evidences of indebtedness in which savings banks may legally invest; *Provided*, That such obligations mature on such dates as will make available without discount such amounts of cash as required;

(3) Obligations of the United States which are redeemable by the U.S. Treasury at the owner's option at fixed redemption values within 1 year from the date of such investment;

(4) Evidences of indebtedness issued by any corporation which meet the requirements of Article V, Sec. 1 (14); *Provided*, That such obligations are not in default as to either principal or interest when acquired, and have a maturity of not more than 12 months from the date of purchase.

#### *General Proviso*

3. Be it *Further provided, however*, That any investments under this Article V shall be made with the exercise of that degree of judgment and care, under circumstances then prevailing, which men of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation but for investment, considering the probable safety of their capital as well as the probable income to be derived.

### ARTICLE VI.—*Available Funds; Custody of Securities; Collections*

#### *Funds for investment*

1. It shall be the duty of each board, commission, department, official, or agency charged with the custody or administration of any State fund to make moneys available for investment as fully as is consistent with the cash requirements of said fund. Monthly, and more often as circumstances require, such official or agency shall notify the State investment officer of the amount available for investment, and the investment shall be made and paid for by warrant drawn by said officer against such fund. Such notification shall include the name and number of the fund for which the investments are to be made, and of the life of the investment if the principal sum is subsequently to be required for meeting obligations.

#### *Surplus cash in the treasury*

2. The State treasurer shall likewise declare as funds available for investment any money in the general fund or special funds of the treasury deemed

unnecessary for operating purposes during the next succeeding 3 or more months.

#### *Custody of securities*

3. All securities purchased or held shall be in the physical custody of the State treasurer who may, with the approval of the State director of finance, deposit with a fiscal agent in any of the financial centers, or with a local bank or trust company, such of said securities as he shall consider advisable to be held in safekeeping by said agent or bank for collection of principal and interest, or of the proceeds of sale thereof.

#### *Collection of income and principal*

4. It shall be the duty of the State treasurer to collect the interest, or other income on, and the principal of such securities in his custody as the said sums become due and payable, and to pay the same, when so collected, into the fund to which the investments belong.

#### *Availability of income for investment*

5. Interest or other income received from the investment of surplus cash in the treasury shall be transferred for credit to the general fund, or the appropriate special fund. All other interest, premium, and income in any form derived from investments, shall be retained by the State treasurer and currently reinvested by the State investment officer on behalf of the fund holding said investments, unless and until the appropriate fund administrative board or head shall issue instructions to the State treasurer as to the transfer or other disposition of such income receipts. Whenever a given investment is owned by two or more funds, the income received shall be prorated in accordance with the ownership of the respective funds.

### ARTICLE VII.—*Records and Reports*

#### *Records of investments*

1. The division of investments shall keep, for each fund for which investments are made, a separate account, to be designated by name and number, which shall record the individual amounts and the totals of all investments belonging to such fund. Every receipt and collection or disbursement when received or made shall be immediately notified to the division for recording to the particular fund to which it belongs.



### *Notification of investments made*

2. The division of investments shall report monthly to each and every interested State official or agency the changes in investments made during the preceding month for their respective fund or funds, and, in addition, shall furnish the details on the investment transactions of any fund as requested by the administrative body or head thereof.

### *Monthly reports*

3. Not later than fifteen (15) days after the close of each month, the State investment officer shall submit to the State director of finance and the State investment council a report of the operations of the division of investments during said month. Each report shall include a detailed summary of investment, reinvestment, purchase, sale, and exchange transactions, setting forth, among other things, the investments bought, sold, and exchanged, the dates thereof, the prices paid and obtained, the names of the dealers involved, and a statement of the funds or accounts referred to herein. Such reports shall also be circulated to a mailing list of investment bankers and brokers recommended by the council, and shall, in addition, be open for inspection to the public and the press in the office of the State investment officer.

## ARTICLE VIII.—*Audit and Review*

### *Post-audit*

1. The State auditor shall be responsible for conducting a continuous post-audit of the investment transactions of the State, and shall submit annually a special report on his findings to the investment council, the Governor, and to the appropriate legislative committee.

### *Annual report*

2. On or before January 1st of each year, and at such other times as it may deem in the public interest, the investment council shall report to the governor and to the legislature with respect to its review of the work of the division of investment.

## ARTICLE IX.—*General Provisions*

### *Act controlling*

1. To the extent that the provisions of this act are inconsistent with the provisions of any other law, the provisions of this act shall be controlling.

*Severability of provisions*

2. If any provision of this act, or the applicability thereof to any person or circumstances, is held invalid, the remainder of this act and the applicability thereof and of such provision to other persons or circumstances shall not be affected thereby.

*Short title*

3. This act may be cited as the "Investment of State Funds Law."

*Effective date*

4. This act shall take effect immediately.

## *Appendix E*

### **PROCEDURE FOR PROJECTING CASH FLOW AND BALANCES**

(Excerpt from "Treasury Cash Management and The Investment of Idle Funds," April 1956. League of California Cities.)

#### *Procedure for Projecting Cash Flow and Balances*

In any case, before embarking on a program for improving cash management, it is important that a definite decision be made as to what individuals and departments are to perform the various operations, and which will review and act on the information compiled. If the program is to be effective, it must be continuous. Procedures should, therefore, be formalized through written administrative regulations and standard practice instructions. If the program is reduced to writing, the individuals and employees will know their specific responsibilities and the schedules that they must meet. Outlining the duties in writing will, in itself, probably result in better review and improvements in methods. Written instructions will also help insure continuation of procedures. Without specific instructions, it often happens that when someone is ill or fails to perform, details are apt to remain undone. There is also an occasional employee who, if he does not understand the overall ramifications of the program, will have a rambling thought or give up the performance of some essential task which may interfere with the effectiveness and success of the program.

#### *Procedural Steps in Forecasting of Cash Position*

In reviewing the specific mechanics for cash management, they have been grouped under seven steps. Actually, many of these steps will be performed concurrently. However, each of the steps represents a major phase of the process, and they are as follows:

Step 1. *Determine the pattern of cash flow in and out of the treasury and analyze bank balances for a long enough period of time to indicate any normal cyclical patterns and identify the normal peaks and low points in balances.*

This analysis can probably best be performed by the treasurer's office. Many treasurers, as a matter of routine, maintain a monthly tabulation of cash flow experience. If this has not already been done, these figures should be reviewed for at least the last 5-year period, with totals tabulated for



deposits, disbursements, and balances for each month and for each fund handled in the treasury. A combined tabulation should also be made of all funds, so that the entire treasury picture with reference to cash flow and balance is clear. An analysis of monthly receipts and disbursements by fund for one year is illustrated in exhibit A.

Step 2. *Break down the totals of receipts and disbursements into their components.* This step can probably best be performed by the accounting office which has the full detail on revenues and expenditures. Breakdown should be made for each major fund and may not be necessary for the smaller trust funds or funds that do not show any marked seasonal fluctuations in receipts and disbursements. Using ordinary stock accountant's working papers, a breakdown by months should be made for 3- to 5-year periods and should include the receipts by major source groups and the disbursements by major object class, such as payroll, retirement contribution, fixed charges, and capital outlay. In segregating the expenditures, it has been the experience that 5 to 12 major classes (depending on the fund) are sufficient, and it is not necessary to tabulate by individual departments. It is better to select object and character classifications where data can be obtained from total fund disbursements, such as payroll. An example of one year's monthly receipts and disbursements analysis for a single fund is shown in exhibit B.

Step 3. *Chart the data obtained in Steps 1 and 2 in a manner that will make clear any cyclical trends in receipts and disbursements.* It will probably be desirable to put 5 years of data on each chart, using a different color or different type of line for each year. In this manner, the lines or bars for each month can be compared directly on the chart with the lines or bars for other months of the entire period studied. The charts and data which are prepared should be reviewed with the top management officials of the unit of government. This will be an excellent means of showing the importance of proper cash control and potential earnings that could be secured through careful planning of investment of temporary surpluses.

Step 4. *Review monthly reports and ledgers of each detailed revenue account classification and prepare what is termed a "factor analysis sheet" for each revenue that has predictable seasonal trends.* The "factor analysis sheet" commonly used is simply a 14-column accounting paper with 48 horizontal line rulings (see exhibit C). One sheet is set up for each detailed revenue account which examination has shown to have a definite seasonal trend in receipts. Each of the fourteen vertical columns is headed by an indication of the fiscal year (a). The sheets are set up originally with the first three columns containing data for 3 prior years, thus providing capacity for entry of 11 future years of experience. Each fiscal year column in turn is divided into two sections. The first—left-hand part of the column (b)—is used to enter the percentage revenue realized each month of the annual total. The right-hand portion of the column (c) is used for entry of cumu-

EXHIBIT B.—*Analysis of Monthly Receipts and Disbursements—General Fund—1954-55*

[Dollars]

Item	July	August	September	October	November	December	January	February	March	April	May	June	Total
<b>Receipts by source:</b>													
General property tax.....			60	176	6,755	57,097	15,000	108,536		760	56,212	10,000	254,596
Sales and use tax.....	6,659	5,659	6,930	8,965	18,083	10,115	20,278	11,218	19,907	10,575	12,697	8,944	140,030
Franchises.....									6,955		13,055		20,010
Licenses and permits.....	1,822	2,454	2,367	2,405	3,251	2,713	20,457	11,750	6,134	2,885	3,406	5,082	64,726
Fines and forfeitures.....	265	284	341	437	354	493	208	218	265	324	619	924	4,732
Revenue from use of money and property.....	675	675	675	675	675	986	2,750	675	675	675	3,638	1,848	14,622
In lieu tax.....		27,500										128,690	156,190
Charges and fees for current service.....	2,585	19,057	3,218	3,962	2,475	4,441	2,000	1,895	8,373	4,722	39,800	12,937	105,465
Other miscellaneous revenue.....	3,863	101	4,291	5,248	9,976	5,925	5,105	1,605	11,164	6,297	10,610	7,470	71,655
<b>Total receipts.....</b>	<b>15,869</b>	<b>55,730</b>	<b>17,882</b>	<b>21,868</b>	<b>41,569</b>	<b>81,770</b>	<b>65,798</b>	<b>135,897</b>	<b>53,473</b>	<b>26,238</b>	<b>140,037</b>	<b>175,895</b>	<b>832,026</b>
<b>Disbursement category:</b>													
Salaries.....	27,625	27,648	28,836	28,369	27,377	27,626	32,288	30,902	30,484	31,806	32,082	56,523	381,566
Service and expense.....	11,546	12,119	30,224	21,564	23,757	2,155	31,502	24,551	9,057	10,187	11,609	63,425	251,696
Equipment rental.....	4,729						9,457					14,271	28,457
Capital outlay.....	1,741	696	3,261	614	1,165		9,992	2,468	1,766	5,140	419	28,339	55,601
<b>Total disbursements.....</b>	<b>45,641</b>	<b>40,463</b>	<b>62,321</b>	<b>50,547</b>	<b>52,299</b>	<b>29,781</b>	<b>83,239</b>	<b>57,921</b>	<b>41,307</b>	<b>47,133</b>	<b>44,110</b>	<b>162,558</b>	<b>717,320</b>
Surplus or deficit.....	-29,772	+15,267	-44,439	-28,679	-10,730	+51,989	-17,441	+77,976	+12,166	-20,895	+95,927	+13,337	+114,706
Closing balance.....	120,453	135,720	91,281	65,602	51,872	103,861	86,420	164,396	176,562	155,667	251,594	264,931	264,931
(July 1, 1954 opening balance:150,225.)													

EXHIBIT C.—Factor Analysis Sheet—Dog Licenses

1952-53 (a)		1953-54		1954-55		Months (d)
Percent for month (b)	Percent to date (c)					
2.4	2.4	1.3	1.3	5.3	5.3	July
1.9	4.3	1.0	2.3	1.1	6.4	August
1.4	5.7	.8	3.1	.8	7.2	September
1.3	7.0	.9	4.0	.6	7.8	October
1.4	8.4	.7	4.7	.5	8.3	November
7.1	15.5	9.8	14.0	.9	9.2	December
19.6	35.1	17.3	31.8	31.9	41.1	January
24.2	59.3	15.1	46.9	24.4	65.5	February
8.7	68.0	21.1	68.0	12.6	78.1	March
16.0	84.0	11.1	79.1	9.3	87.4	April
10.4	94.4	12.3	91.4	7.6	95.0	May
5.6	100.0	8.6	100.0	5.0	100.0	June
Total revenue receipts for year (e)						
\$42,769.50		\$47,244.49		\$67,061.00		
						3-year moving average (f)
						3.0
						1.3
						1.0
						1.0
						.8
						5.8
						23.1
						21.2
						14.2
						12.1
						10.1
						6.4
						3.0
						4.3
						5.3
						6.3
						7.1
						12.9
						36.0
						57.2
						71.4
						83.5
						93.6
						100.0
						July
						August
						September
						October
						November
						December
						January
						February
						March
						April
						May
						June

lative percentage realization. There is no entry for the total dollar amounts received each month on the historical data. The reason for this is that the objective is percentage realization, rather than dollar amounts. By going through the detail revenue reports, an employee can utilize a calculating machine to compute the percentages directly from the reports and enter them on the analysis sheets, thus saving unnecessary transcription work.

The entries which have been described are made on the 12 horizontally ruled lines in the top portion of the form, with one line used for each month. (d) Below this section are entered the total dollar receipts for the revenue source for the year. (e) Below that is an area of 12 more horizontal rulings, in which are computed and entered for each year the average of each month's percentage figure for the 3 prior years. (f) In this manner a series of moving averages is maintained. By making analysis of individual revenue accounts as to percentage of total annual revenue that has been realized each month, data are obtained that can be applied in estimating probable monthly receipts in future years. Unless some change in law is made or a major change occurs in economic conditions, the cyclical patterns of receipts for individual revenue source will generally be fairly consistent, and thus predictable. Once these factor tables are established, it is also possible to revise budget revenue estimates quickly during the course of the year by

merely dividing the receipts to date by the factor of expected percentage realization to date.

Step 5. *Prepare projections for each fund, and for all funds combined, of monthly receipts, disbursements and estimated balances.* The basic guide for the fund and total projections will be the past experience analysis and revenue factor sheets. The projection of receipts and disbursements should be done in much the same detail and form as the historical analysis, with receipts by sources, and expenditures by major object classification. The percentage factors by revenue account will be guides to many of the receipt projections. However, it must be remembered that adjustments must be made for changes that occur in revenue structure, methods of administration, and other conditions which were nonexistent at the time the historical data were prepared. Similarly, expenditure projections should always be carefully considered. Some classes of disbursements are readily assessable such as payroll, supplies, services, and other relatively fixed costs. Monthly cash requirements for items like bond interest and redemption, of course, can be easily ascertained. However, many categories are not so easily determined, such as expenditures for land, buildings, and equipment. Projections on the major variable expenditure items can best be made through discussion and analysis prepared by the departments directly responsible for their administration.

Projections of the type described can be made for different periods of time. It is recommended that an annual projection be prepared prior to the beginning of the fiscal year. At this time, the work sheets should provide at least three horizontal lines for each item (see exhibit D). The first line will be used to record the actual experience and will be entered at the close of the books each month. The second line will be used to enter the annual estimated projection figures; the third and subsequent blank lines will be reserved for entering revised projections made at least quarterly and, if necessary, they are made monthly.

EXHIBIT D.—*Annual Projection Sheet—Revenues*

	Total	July	August	June
Dog licenses—account No. 1-230, actual.....	(a) \$67,051	\$3,555	\$738	\$3,354
Original projection.....	(b) 64,860	3,300	645	3,400
Revised projections.....	(c) 21,546	1,140	1,950	2,758
Plumbing permits—account No. 1-232, actual.....				
Original projection.....	20,720	1,200	1,750	2,700
Revised projections.....	18,239,534	715,044	1,084,623	2,499,072
Total—general fund revenues, actual.....				
Original projection.....	16,462,407	687,426	1,210,943	2,178,475
Revised projections.....				

The above illustrations are samples of the manner in which all revenue sources (and expenditure classifications) are estimated at the beginning of a fiscal year, with the resultant figure for total revenues and expenditures for each fund and for the total of all funds. Where revised quarterly projections are in order, they may be inserted on line marked (c) and new totals carried forward.



For the purpose of revising and keeping up-to-date the projections of disbursement requirements, particular attention should be given to any major construction project payment requirements. It is possible to develop a simple form to be sent to the contractor when a construction bid is awarded (see exhibit E). On this form the contractor can indicate what he believes will be his progress earnings per month. After review of this form by the city engineer or the utility department administering the contract, it will be used for revising the projection figures. Blank columns can be provided on the form for entry of revised estimates made by the supervising engineer as the job progresses.

*Step 6. Establish a program of regular review of the annual and quarterly projections of monthly receipts and disbursements and use the data for controlling cash flow where possible.* In this connection, referral is made to a responsibility of the budget administration authority to schedule major construction projects, changes in activities, and operations of departments so as to minimize the cash problem during "lean periods." This review should also indicate the need and provide the basis for advance planning of temporary loans or of investments. Such investment plans are more likely to be executed if policies are set well in advance, particularly as to the proper level for maintenance of active bank balances.

*Step 7. Establish the policies and procedural mechanics for cash analysis and control on a daily, weekly, or other short-term period within each month.* It is in this area of short-term cash analysis and control that most finance officers can improve their practices. With proper methods, it is entirely possible for a city to predict disbursement volumes several days or weeks in advance. For many types of disbursements, a little analysis will show what cash flows are to be anticipated. This is true because such things as payrolls are paid out on regular recurring schedules, as are many types of vendor's payments. The disbursements that are not cyclical in nature can be predicted (usually some days in advance) by establishing notice procedures on major items so that the person responsible for watching cash flow is notified as soon as deliveries are received or as progress on a contract job is known. The section of the accountant's office that handles auditing of payments and receives delivery certifications from departments should be instructed to flag all major items and provide advance notification on major disbursements. Similarly, offices such as the city engineer, supervising major contracts, can arrange to advise the accounting office or treasury as soon as construction inspectors have determined the percentage of progress on which payment will be made. This information can be obtained at least 10 days to 2 weeks prior to the handling of the warrant or check.

## EXHIBIT E.—Contractor's Estimated Payment Schedule

Contractor:  
 Address:  
 Estimated Starting Time:

P.O. No.  
 Name of Project:  
 Estimated Completion Date:

### PAYMENTS

Month	Estimated percent to be completed	Estimated to be earned for month	10 percent deduction (estimated withheld)	Estimated to be charged for month
January.....				
February.....				
March.....				
April.....				
May.....				
June.....				
July.....				
August.....				
September.....				
October.....				
November.....				
December.....				
Next Year.....				
Total.....				

## *Appendix F*

### **DETERMINATION OF AMOUNT OF CASH TO BE MAINTAINED IN ACTIVE BANK BALANCES**

(Excerpt from "Short-Term Investment of Idle Funds," March 1958,  
International City Managers' Association)

#### *Determination of Amount of Cash To Be Maintained in Active Bank Balances*

Once the finance officer has established a program of projection of cash flow and has tested its reliability, it will be possible to predict with reasonable accuracy the probable cash balances of the various funds and the probable cash totals to be expected in the treasury. If it has been possible to develop day-to-day procedures for cash control and review, they will reveal a great deal about the probable daily balances long enough ahead to plan utilization of funds for very short-term investment.

Before the release of these funds for investment, however, it is necessary that policies be established as to the amount of balances which should be retained in active bank accounts to handle transaction volumes. Obviously, the proper amount to be maintained in active bank balances is not quite as simple to ascertain as might be believed. It is not enough to think that the only requirement is to have a balance great enough to cover the checks or warrants written. Although this consideration is ample for most individual depositors, it oversimplifies the problem of the governmental treasurer. It is just as true, however, that funds not needed to maintain proper active bank balances certainly should never be left in a noninterest bearing account to allow the bank to obtain earnings which might properly be obtained for the governmental treasury.

For instance, blanket use of a fixed ratio between active and inactive accounts is not always the proper approach, particularly for the average-sized and larger cities. These ratios vary from one-to-one up to three or four-to-one, depending on locality, competition, size of account, and many other factors. Simply stated, a one-for-one ratio means that the city must keep on deposit one dollar in an active (non-interest bearing) account for each dollar maintained in an inactive (interest bearing) account.

Obviously, the "effective rate of return" to the city on its total amount of money on deposit is substantially reduced. As an example of the one-to-one ratio, if it is assumed that a bank is paying 1 percent on an inactive account

and nothing on an equal amount of active deposit, then the "effective rate of return" to the city on all its bank accounts is only one-half of 1 percent. As the ratio is increased to allow a greater amount of inactive deposits per each dollar of active deposit, the over-all rate of return on total deposited funds is increased proportionately.

It would appear that the proper approach to this problem is to discuss with bank authorities the mutual interests which prevail. They should be asked to present their policy and views with regard to compensating balances for municipal deposits. The treasurer, however, has a responsibility for satisfying himself in a factual way as to validity of the policy suggestions made by the bank.

Basically, the treasurer should feel no responsibility for maintaining active deposits other than amounts sufficient to compensate the banks for the work they perform which will provide reasonable commercial profit margin. Most banks calculate that they will earn from an active account some 1.5 to 2.0 percent of the average balance, less what is termed as the "float." The "float" is, generally speaking, the checks which the depositor has deposited to the credit of his account but which have not cleared to bank of origin. From this earning balance, the bank must subtract the costs of handling the customer's business. There are well accepted methods for calculating the costs of handling a customer's account for the normal, commercial-type depositor.

In the case of a municipality, there must be added to the normal account costs the value of special services performed by the bank. For example, the bank is certainly entitled to reasonable compensation if it takes bids on investments, maintains custody for securities, makes special pickups of money, delivers bonds and securities, treats the city as a preferred depositor by pledging securities to cover its deposits and, in some cases, if warrants are still used for payment rather than checks, carries a substantial additional "float" on the city's account beyond that normal for a commercial account.

Banks also often render valuable services in connection with the administration of city debt, including acting as trustee for bond issues; fiscal paying agent for bonds and coupons; agent to receive, examine, and deliver issues of municipal bonds; handling of exchange of maturing and called bonds for the new issues; dissemination of municipal financial data in connection with bond issues; and furnishing one of the major markets for purchase of municipal bond issues. Many valuable services also are rendered in connection with the investment of temporary cash surpluses of the municipality.

It is suggested that, after the special factors are considered, the balance of the cost of handling the city account should be figured on the same basis on which commercial account costs are valued. It would be well for finance officers to familiarize themselves with the methods used in

calculating the cost of handling an account. They are, therefore, reviewed as follows:

1. The bank first prepares an analysis sheet for the account. Under each column are horizontally ruled lines for each day in the month for tabulating each day's transactions.
2. When the above data have been compiled, earning factors and cost factors are computed approximately as set forth below. Charges in the sample schedule are only generalized examples and will vary, depending on a particular bank's system of analysis:

*Earning Value of Account*

1. Average account balance \_\_\_\_\_
2. Less average dollar amount of checks deposited \_\_\_\_\_
3. Average collected balance \$ \_\_\_\_\_ (Item (1) minus (2))
4. Earning value of account \_\_\_\_\_ (Item 3 x .00125—if based on 1½% per year)

5. *Cost of Handling Account*

- a. Interest on uncollected funds \$ \_\_\_\_\_ at 6% per year  
(Charge if Item 2 exceeds Item 3 only)
- b. Number of deposits @ \$.05 each \_\_\_\_\_
- c. Number of checks deposited or cashed @ \$.15 each \_\_\_\_\_
- d. Cash deposited @ \$.15 per \$1,000 \_\_\_\_\_
- e. Checks paid from account @ \$.035 \_\_\_\_\_
- f. Returned items @ \$.15 \_\_\_\_\_
- g. General account maintenance charge \_\_\_\_\_
- h. Total cost \$ \_\_\_\_\_

(Net account profit or (loss)                      \$ \_\_\_\_\_  
(4 minus 5h)

# Appendix G

## TYPES OF INVESTMENTS

(Excerpt from "Treasury Cash Management and The Investment of Idle Funds," April 1956. League of California Cities.)

### 1. *Time Deposits*

These are commonly known as inactive interest-bearing accounts similar to a savings account and are available to any municipality. First of all, it should be realized that city deposits in a bank are not unregulated since they are governed by Regulation "Q" of the Federal Reserve System and also by sections of the Government Code. As of this writing, municipal deposits in any one bank are limited to the total of capital and surplus of that bank, exclusive of reserves. To the extent that they may be used, however, time deposits are a good source of investment. The principal is as safe as possible, the money is available upon short notice and the earnings are reasonably good. A city desiring to maintain small amounts of interest-bearing money where it might be utilized in a short time, or upon short notice, would do well to place as much as possible in either 30-day or 90-day notice time deposits. Monies which are available for longer periods of time, such as a year or more, may be deposited in one-year-notice time deposits at a slightly higher interest rate. Inactive interest-bearing bank accounts are particularly attractive for smaller cities when temporarily available surpluses are not large enough to justify going through procedures necessary for purchase of U.S. Treasury bills or other types of investments discussed in this report.

Interest rates on time deposits vary, depending on the particular bank, the notice required, the amount of added business involved, and other factors. For many years, most banks have held that municipalities should be governed by the "one-to-one" ratio on their time deposits, as explained earlier in this report. Although many banks still champion this ratio, the more progressive institutions are broadening their view. Some banks have now shifted to a "two-to-one" arrangement (one dollar of commercial deposit for every two dollars of time), or even a "three-to-one" ratio. But the most forward-looking banks will surely have to come to the conclusion reached by the writers. That is, the commercial or active account of a city should be maintained only at a sufficient balance level to compensate the bank for the services required (checks written, deposits taken in, returned items processed, statements rendered, special services and advice given). Full recognition should be allowed in this balance to the bank's problems of

“float,” unemployable funds, community service, and other factors. But once this proper level of commercial balance has been determined to the mutual satisfaction of both parties, all other funds should be placed in interest-bearing accounts without regard to ratios or any other outside factors. The cities are just as entitled to earn money on their funds as are business corporations or individuals; indeed, they would be doing their taxpayer constituents a disservice if they failed in this regard. This category of time deposits represents the largest investment medium for municipal funds. For many of the smaller cities, these deposits normally may constitute about the *only* usable type of investment.

## 2. *Government Securities*

One of the greatest sources of earnings for all sizes and types of municipalities is in the field of “governments.” These securities of the United States Treasury are backed by the full faith and resources of the U.S. Government and are approved channels of investment under all circumstances. They reflect the current level of interest rates because they are not subject to any of the hazards of credit risk or quality deterioration. They are issued in any one of several forms, among which are bonds, notes, certificates of indebtedness, 90-day bills, tax-anticipation notes, and other types. Maturities vary from the short-term bills to long-term bonds of 20 and 30 years or more. Some issues are callable by the Government prior to maturity, others are not. Some are offered on the open market for cash, while others are available by exchange of an issue already held. Some are purchased at face or par value, others are bought at a discount. Some securities have coupons attached, others do not. The varieties and types are numerous and constitute another reason why proper advice from a qualified bank or broker is necessary before entering the market.

*Treasury Bills.*—Perhaps the greatest use is made of the U.S. Treasury bills, which are limited in maturity to a period of 1 year or less. They are issued on a discount basis, and the return on the investment is the appreciation between the price at which they are purchased and their maturity value of 100. With the exception of tax anticipation bills issued from time to time to finance temporary Treasury needs, bills are currently issued with a maturity of 90 to 92 days. When a holiday does not interfere, the maturity is 91 days. At present, there are 13 weekly series, most of them in the amount of \$1½ billion each. They are offered at a competitive auction each Monday for payment every Thursday. Bills are held primarily by commercial banks, the Federal Reserve System, and nonfinancial corporations, although at times, long-term investors such as insurance companies and savings banks use them for the employment of temporary funds. Bills provide a highly liquid investment for short-term funds with relatively little market risk. They are particularly appealing to a small city with limited investable funds and a short-range spending program. They do not have to be held long to make a profit \* \* \* and they satisfy all the

basic ingredients of a proper investment program. Because of the necessary functions which must be performed in order to subscribe for, hold, and sell Treasury bills, it is not normally a satisfactory source of investment unless a city can make a purchase at any one time of at least a minimum amount of approximately \$50,000. For exact calculations as to the minimum purchase in each specific situation, any bank or investment counselor will be glad to assist.

*Certificates of Indebtedness.*—Treasury certificates of indebtedness are also issued with a maturity not over 1 year. Those outstanding at the present time, with the exception of one tax anticipation series, have been issued for that period. They carry one coupon payable at maturity. All regular series of certificates of indebtedness now outstanding were issued in refundings of maturing Treasury securities. In order to assure a successful refunding, they have been priced when offered to yield a return which would result in some premium in the open market. This resulted in maturing issues having a market, or “right” value above par because of this exchange privilege. For this reason, certificates of indebtedness frequently sell in the market at a yield which appears on the surface less attractive, when maturity is considered, than do the Treasury bills which have no right value. The same fact influences the market prices of Treasury notes and bonds as they near maturity. While not quite as liquid as Treasury bills, experience has shown that certificates of indebtedness can, under almost any circumstances, be quickly and easily liquidated when the holder requires cash.

*Treasury Notes.*—For those cities whose available resources allow them to plan a little further in advance, the longer Government securities provide more possibilities for increased earnings. Treasury notes are issued with a maturity of longer than 1 year, but not more than 5 years. They are of primary interest when cash requirements fit the particular maturities. A more common purchase, however, is that of U.S. Treasury bonds.

*Treasury Bonds.*—Treasury bonds are not restricted by law as to date of maturity. It has, nevertheless, been the policy to issue them only with maturities of 5 years or longer. Intermediate maturities, that is, those originally offered to mature in from 5 to 10 years, are purchased largely by commercial banks. Those with maturities over 10 years are held principally by financial institutions, such as savings banks, savings and loan associations, insurance companies, private pension funds, public pension funds, and other public funds of various types.

Since it is axiomatic that “the longer the maturity, the greater the risk,” it is not always possible to manipulate the notes and bonds to make a spot profit whenever desired. However, they are just as safe as any other types when held to maturity. The amount of funds available for investment and the length of the potential investment period determine the extent to which



these securities may be purchased. They are ideal for pension funds, bond redemption and interest funds, or any other funds where the principal is not needed until some future date.

*Series "J" Savings Bonds.*—Some cities have used to advantage the new Series "J" Savings Bonds—one of the many nonmarketable issues of the Government. These issues are redeemable at the option of the holder, either on demand or after a fixed period of notice, but cannot be transferred from one holder to another. For those municipalities who have nonfluctuating funds available for long-term investment, the interest return from the series "J" savings bonds is excellent.

### 3. *Municipal Securities*

Bonds issued by States and their political subdivisions, i.e., cities, counties, school districts, special districts of all kinds, and public authorities, are known as "municipals." These bonds have one thing in common, the interest they bear is exempt from Federal income taxes. As a result thereof, these bonds are sought by individual and corporate investors whose incomes are taxed at high rates. Yields obtainable on the better grade municipal bonds are, therefore, normally lower than on U.S. Governments which are fully taxable. (A small and shrinking portion of the Federal debt is partially tax-exempt.) As the earnings of city funds are not subject to Federal taxes, there is no incentive for the city finance officer to pay a premium for tax-exempt income.

There are times when, due to the heavy supply of municipal bonds or other market factors, *sound* municipals are obtainable at yields comparable to, or better than, those for similar maturities of Governments. At such times, the city finance officer may be justified in purchasing municipal bonds.

There are two principal types of municipals, (1) general obligation, and (2) revenue bonds. The first are secured by the general taxing power of the issuing entity. (In some States this taxing power has constitutional or statutory limits.) Revenue bonds are secured by the pledge of the earnings of a publicly owned utility or enterprise, such as a water system, a toll road or toll bridge, or parking facilities; or sometimes, particularly in the case of a State, certain specific taxes only may be the sole source of debt support, such as a gasoline tax or cigarette tax.

Revenue bonds carry, in most cases, higher yields than general obligation bonds of the same obligor. Revenue bonds must be judged on a basis comparable to the selection of bonds of a private corporation and, consequently, must be chosen with great care. Very sound issues are available, however, and opportunities for profitable investment of public funds may be found. Expert advice is a necessity when selecting municipal bond issues and is especially so in the revenue bond field.





