

MEMORANDUM IN SUPPORT

RE: A. 9909 (Hoyt)/S. 6929 (Foley) AN ACT to amend the general municipal law, in relation to expanding the definition of banking entities authorized for the deposit of temporary investments funds

The New York Bankers Association supports this legislation that would authorize local governments to deposit funds in local New York commercial banks and thrift institutions that could then be covered by a reciprocal matching deposit-taking program in which federal deposit insurance coverage in excess of the current \$250,000 limit is provided. This legislation will enhance the safety and security of local government deposits, reduce the cost and burden of managing collateral backing local government deposits and increase efficiency in the local government deposit market. It would benefit both municipal depositors and their depository institutions. We strongly urge that it be approved. Our Association is comprised of the community, regional and money center commercial banks and thrift institutions doing business in New York State. Our members employ approximately 250,000 New Yorkers and have assets in excess of \$9 trillion.

New York's General Municipal Law provides an extremely effective system of safeguarding the deposits of New York's local governments. Every dollar on deposit in excess of deposit insurance limits must be fully collateralized by government securities or other readily marketable and fully valued collateral. No government deposit protected by this system has ever been lost.

However, the system comes with a significant cost. Because government securities pay rates of interest sometimes far below alternative investments, they earn very little for depository banks that must use them for collateral. In addition, the law requires that local governments and their depositories must manage the collateral on a periodic basis, ensuring that it remains liquid and that its principal amount remains more than adequate to cover all deposits. The cost of managing the collateral, in personnel time and administrative recordkeeping, can be considerable.

As a result, local governments, which typically bid out their deposits, often find bidders willing to pay less than they might on deposits of comparable amounts and maturities which do not have to be fully collateralized. Importantly, because deposits covered by FDIC insurance are not required to be collateralized, those portions of local government funds can be managed more efficiently and less expensively than can deposits requiring collateral.

In the past several years, a new program has been developed by a number of financial services companies to allow banks to match reciprocal deposits with each other. The programs permit a local bank to accept a large municipal deposit, maintain the entire deposit on behalf of the local government, while parceling out portions of the deposit, each below the deposit insurance limit, to other banks across the country. In return, the other banks place matching deposits, with the same terms, maturity and interest rate, in

the New York bank. As a result, every dollar on deposit, up to the limits of the programs, becomes fully insured by the FDIC. As is well known, the FDIC is backed by the full faith and credit of the federal government and no depositor has ever lost any funds covered by the deposit insurance limit during the entire more than 75-year history of the FDIC.

These matching reciprocal deposit programs have now been authorized in 45 states. This legislation would allow New York local governments to take advantage of the program by placing deposits through a New York bank that would then be matched by reciprocal deposits in other banks. Deposit insurance coverage for accounts on deposit would increase enormously, at the same time as the need for collateralization of deposits would be commensurately reduced. This outcome would be beneficial to both depository banks, which could maintain deposit insurance, in most instances, far more cheaply than collateral, and for local governments, which would find bidders potentially offering more attractive rates while being relieved of the cost of managing collateral.

For these reasons, the New York Bankers Association supports this legislation and urges that it be approved.