Approved: March 1, 2001
Date

MINUTES OF THE HOUSE COMMITTEE ON LOCAL GOVERNMENT.

The meeting was called to order by Chairperson Rep. Gerry Ray at 3:30 p.m. on January 30, 2001 in Room 519-S of the Capitol.

All members were present except: Rep. Toplikar

Committee staff present: Theresa Kiernan, Revisor
Mike Heim, Research
Kay Dick, Committee Secretary

Conferees appearing before the committee:
Proponents:
Don Moler, Executive Director, League of Kansas Municipalities
Randy Allen, Executive Director, Kansas County Association
David Scott, Manager of Finance & Accounting, City of Overland Park
Charles Henry, Treasurer, Unified Government for Wyandotte Co.
Thomas Franzen, Johnson County Treasurer's Office
Rodney Franz, Director of Finance, City of Salina
Dennis Howard, Chief Financial Officer, City of Lenexa
Mike Taylor, Government Relations Director, City of Wichita
Carla Palmer, City Treasurer of Wichita
David Harris, Bank of America
Phil Ekstrom, President, First Bank, Topeka
Donald Johnston, Director, Commerce Bank, Lawrence
Norman Wilks, Attorney, Kansas Association of School Boards
Michael Pepoon, Director of Government Relations, Sedgwick Co.
Donald Seifert, Policy Development Leader, City of Olathe

Opponents:
Bob Kennedy, Executive Directory, Community Bankers Association
D. Max Fuller, President, The Stockgrowers State Bank, Maple Hill
Steve Hadlke, CEO, Union State Bank, Everest
Chuck Stones, Senior Vice President, Kansas Bankers Association

Others attending: See Attached list.

Jonathan Small, National Multi Housing Council, requested an introduce a rent control preemption bill.

Without objection it would be introduced as a committee bill.

Rep. Dillmore, 92nd Dist. requested a bill concerning liquor tax and allocation. A motion in favor was made and seconded. Motion passed with no opposition.

Hearing was opened on:

HB 2086 - concerning municipalities; relating to depositories for public funds

Don Moler, League of Kansas Municipalities, summarized the bill and presented his testimony. He spoke of how the bill proves greater flexibility for cities, counties and other local unit of government, by allowing taxpayer dollars to be maximized. "Cities should be authorized to designate any federal or state chartered financial institution as a depository for city funds." He urged the Committee to be very careful in accepting amendments to this legislation. "Ultimately this is a bill which promotes competition and thereby maximizes the public's dollar." (attachment #1)

Randy Allen, Kansas Association of Counties, expressed support for the bill, which would give the counties additional options in the deposit of their public funds. KAC views this as an issue of local control. (attachment #2)

David Scott, Manager of Finance & Accounting for the City of Overland Park, expressed that Overland Park supports **HB 2086** for reasons that it increases competition among financial institutions. This will allow local government to receive higher interest rates and thus, property taxes will decrease. He also stated, that the bill would provide an economic buffer to local governments during a slow-down in local economy. By allowing the financial institutions outside of Kansas to bid, local governments can benefit from others not affected by slow economic times Also, pointing out an opportunity to increase the diversification among financial institutions, He concluded that this bill would eliminate the artificial investment barriers existing today - and allow for competitive investment markets to better serve the tax payers of Kansas. (attachment #3)

Charles Henry, Director of Revenue/treasury for the Unified Government of Wyandotte County, testified in favor of **HB 2086.** He concluded by saying that this bill will offer the Unified Government the chance to earn additional investment income at no cost to the taxpayer. Because the law and our policies remain unchanged regarding depository security, the taxpayers are not at risk. (attachment #4)

Thomas Franzen, Chief Deputy County Treasurer, Johnson Co. appeared and testified in support of the bill, stating that it would allow governmental entities to conduct business at the lowest possible cost, thereby passing potential savings onto taxpayers in the form of a reduced mill levy. (Attachment #5)

Chair introduced another proponent, Rod Franz, Director of Finance, City of Salina. He testified that there were five specific reasons for supporting HB 2086. 1] It maintains the safety of public funds. 2] It makes the two statutes consistent with one another. 3] It simplifies the process. 4] Diversification of the investment portfolio is a safety and liquidity feature. 5] It enhances the market enabling better rates with a more open and unrestricted market. (Attachment #6)

Dennis Howard, Chief Financial Officer, City of Lenexa, testified on behalf of the City, expressing support for HB 2086. (Attachment #7)

Mike Taylor, Government Relations Director for the City of Wichita, stated, You will have two separate testimonies, one from Carla Palmer, City Treasurer and one from myself, and in the interest of time I'm going to consolidate and present both testimonies. Although Carla is here for questions later as she has more technical expertise in this than I do." He testified that managing public money involves a special trust and requires public officials to use caution, diligence and expertise to make sure those funds are invested in the public interest. The current statute limits municipalities from properly diversifying their investment portfolio, based on local banks need for funds. Under the new legislation this would allow municipalities to diversify based on prudent investment practices. Mandatory "hometown banking" is a thing of the past. (attachment #8 & #8a)

David Harris, Bank of America, gave testimony in support of **HB 2086.** He emphasized that this bill will not dictate where any Municipality must bank, only allowing a more competitive environment from which Municipalities may select their banking services. (attachment #9)

Phil Ekstrom, President, Firstar Bank, testified in favor of **HB 2086.** He stated that deposits have decreased due to bank and non-bank competition. "This is a problem all bankers face." He summarized by saying, "Competition is good and healthy. Competition keeps us sharp and aggressive. Not allowing banks with out of state charters to offer certain services to public fund customers would reduce interest received by the public entity due to reduced competition. (attachment # 10)

Don Johnston, Director of Commerce Bank of Lawrence gave testimony in support of **HB 2086.** He stated that if the proposed legislation were approved, banks would be free to utilize a system-wide array of banking and investment tools to the fullest advantage for our municipal customers. They could bid for local funds in a much more competitive manner, allowing constituent municipalities to reap the benefit. (attachment #11)

Norman Wilks, Attorney, Kansas Association of School Boards, testified in support of **HB 2086**. He stated that this bill represents a longstanding policy of the Kansas Association of School Boards. (attachment #12)

Mike Pepoon, Director of Government Relation, gave testimony in support of **HB 2086** on behalf of Sedgwick County. He emphasized that the effect of this legislation would give cities and counties more options to take care of their banking needs and create an environment of more competition from such banks for these services. (attachment #13)

Don Seifert, Policy Development Leader, testified in favor of **HB 2086** on behalf of the city of Olathe. He indicated that the city believes this bill is good public policy, and gave several reason. (attachment #14)

Chair recognized that this was the conclusion of proponents for **HB 2086** and announce moving on to the opponents for the bill.

Bob Kennedy, Community Bankers Association, briefly stated the position of the association representing other bankers in the association. He explained that 40% of the association members were small town banks(in towns of 1,000 or less) This bill would create another drain on the deposits, further weakening the ability to satisfy the capital needs of the local community. (attachment #15)

Max Fuller, President of The Stockgrowers State Bank, Maple Hill, gave testimony in opposition to **HB 2086** asking that the committee amend the bill to leave the law in regard to Idle Funds in its present form. He started that the State Idle Funds are an important source of funds for most Community Banks in Kansas. (attachment #16)

Steve Handke, CEO, Union State Bank, Everest, stated that he would provide written testimony at a later date. Mr. Handke testified in opposition of **HB 2086** stating that it is poor public policy for the State of Kansas. He also addressed some of the economic terms heard from the counties and cities.

Chuck Stones, Senior Vice President, Kansas Bankers Association, appeared before the committee in opposition to **HB 2086.** He said that Kansas taxpayers money should stay in Kansas for the benefit of the taxpayers. He also declared that it is very evident that Kansas is merely acting as a deposit collecting area for some of the large multi-state banking operations. He went on to say that it is not the local unit of governments' money. It is not about competition. There is not a need for this legislation. He continued to expand on how many Kansas banks depend on local public funds as a stable base of deposits in order to meet the needs of their communities. He said that the association feels that this legislation is not in the best economic interest of Kansas and its taxpayers. He also gave suggested amendments to **HB 2086.** (attachment #17)

Chair Ray called attention to a letter from Jack Ford, Mayor of Kingman City supporting the bill. (attachment #18) And a letter from Bruce Morgan, Chairman, President & CEO of Valley State Bank in opposition to **HB 2086.** (attachment #19)

Both proponent and opponent conferees responded to questions asked by the committee.

Chair Ray closed the hearing on **HB 2086.**

Meeting was adjourned at 5:10. Next scheduled meeting is February 1, 2001.

HOUSE LOCAL GOVERNMENT COMMITTEE
GUEST LIST
JANUARY 30, 2001

[PLEASE PRINT YOUR NAME]	[REPRESENTING]
Don Moler	LKM
Sandy Jacquot	LKM
David Scott	Overland Park
Kelly Kultala	City of Overland Park
Norm Wilks	KASB
Rod Franz	KSGFOA / City of Salina
Mike Taylor	City of Wichita
Carla Palmer	City of Wichita
Mike Pepoon	Sedgwick County
David Harris	Bank of America
Phil Ekstrom	Firstar
Charles Henry	Unified Government WYCO/KCK
Dennis Howard	City of Lenexa
Marla Goodrich	PMIB
Derl Treff	PMIB
Ashley K Sherard	Johnson County
Tom Franzen	Johnson County
Ron Appletoft	Water Dist. No 1 of JoCo.
Don Seifert	City of Olathe
Sonya Allen	Office of the State Bank Commissioner
Judi Stork	"
Bob Kennedy	Community Bankers Assn. of KS

HOUSE LOCAL GOVERNMENT COMMITTEE
GUEST LIST
JANUARY 30, 2001

[PLEASE PRINT YOUR NAME]	[REPRESENTING]
D. Max Fuller	Stockgrowers State Bank / CBS
George Barbee	Community Bankers
Chuck Stones	KBA
Whitney Damron	WYCO/KC,KS
Kathy Olsen	KBA
Randy Allen	Ks. Assn. of Counties
DON JOHNSTON	COMMERCE BANK N.A.
Ron Gaches	CBBA
John D. Pinegar	Pinegar Smith Co.

LKM
League of Kansas Municipalities

300 SW 8th Avenue
Topeka, Kansas 66603-3912
Phone: (785) 354-9565
Fax: (785) 354-4186

To: House Local Government Committee

From: Don Moler, Executive Director

RE: Support for HB 2086

Date: January 30, 2001

First, I would like to thank the Committee for allowing the League to testify today in support of HB 2086. This bill represents a cornerstone of the League's legislative priorities for the 2001 legislative session. HB 2086 provides greater flexibility for cities, counties, and other local units of government, by allowing taxpayer dollars to be maximized. The convention of voting delegates, made up of League member cities, adopted the following as part of our action agenda:

> *"Cities should be authorized to designate any federal or state chartered financial institution as a depository for city funds."*

Competition, Competition, Competition

We believe HB 2086 accomplishes this very straight-forward goal. It has been brewing as an issue of concern to local governments for several years as a result of the continuing changes in the banking industry. We now have a situation where many of our larger units of government find that most of the banks which would logically be depositories for their funds are no longer eligible to hold these funds because they are not state chartered banks and do not have a main office located in the state of Kansas. This legislation will be beneficial for both large and small cities and their taxpayers. Specifically, allowing banks which are not chartered in Kansas to bid on public moneys would reintroduce competition into the state banking market and thus allow local units to maximize the return on the public's tax dollar. This is a point which cannot be overstated as the difference of a .5% or 1% interest, when investing millions of dollars, is a sizeable amount of money. It should also be stressed that the safety of the public's money will not be impacted. This is the case because the rules which apply to investments today would apply to investments tomorrow. The only difference would be fostering competition by allowing more banks to be eligible to bid on active and inactive funds of local governments in Kansas.

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Attachment 1

Protectionism

The existing law in this area is totally protectionist in nature. It is our understanding that 49 states currently do not engage in such protectionist policy and allow competition to prevail. I am sure that some argument will be made today concerning the fact that if the state does not have a law in place to protect Kansas chartered banks, that the passage of this legislation will be their death knell. We do not believe this to be the case simply because the decision as to where to make investments of public tax dollars will still be in the hands of locally-elected governing bodies. People living in the cities and counties in which these banks currently operate would seem to have the greatest stake in seeing that the banks remain strong and vibrant. Thus, rather than putting these banks out of business, I would suggest that the actual result will be to simply add an element of competition to the market. Thus, the ultimate choice about placement of public funds will be left with locally-elected government officials, who will still, at their own discretion, have the option of placing funds in their local bank.

State Currently Has Authority to Invest in Out-Of-State Banks

While some may characterize this legislation as detrimental to Kansas, we would point out the simple fact that the State of Kansas already has the authority to invest in out-of-state banks and we are merely asking for the same type of flexibility already granted to the State itself. We are not asking for **any** expansion of investment authority, only the option of placing the public's tax dollars where they will receive the highest and best return, much like the State of Kansas does today.

Conclusion

In conclusion, I would urge the Committee to be very careful in accepting amendments to this legislation. While there may be some language which is necessary to further the plan envisioned here, if amendments are placed on this bill which would loosen the investment laws of the State of Kansas, an entirely new element will enter into the debate. At its core, this is a very simple piece of legislation designed only to give more flexibility to local governments. It is not a debate about investment policy nor is it a debate about the safety of public funds.

Ultimately this is a bill which promotes competition and thereby maximizes the public's dollar. We believe this legislation to be in the public's best interest and would urge the Committee to report it favorably to the House floor.

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KANSAS ASSOCIATION OF COUNTIES

TESTIMONY
concerning House Bill No. 2086
Depositories for Public Funds

Presented by Randy Allen, Executive Director
Kansas Association of Counties
January 30, 2001

Madam Chair and members of the committee, my name is Randy Allen, Executive Director of the Kansas Association of Counties. I am here today to express support for House Bill No. 2086, which would provide additional options for counties in the deposit of their public funds.

Currently, counties are barred from designating banks without charters or home offices in the state of Kansas as their depositories for county funds. This has the effect of stifling competition among banks for counties' financial services. Our primary reason for supporting HB 2086 is to give county decision-makers who are the most sensitive to local concerns and local taxpayers the **option** to deposit county funds in a bank(s)s which provides the most optimal return and best level of services to the county - regardless of where it is chartered or where its home office is located.

HB 2086 would not restrict any county from continuing to designate a local, Kansas-chartered bank as its depository. In fact, we envision a continued sensitivity of boards of county commissioners to doing business locally as much as possible while at the same time protecting local financial interests by securing the best advantage for local taxpayers. Currently, the playing field is not level and non-Kansas chartered banks are at a competitive disadvantage. More importantly, local taxpayers are at a disadvantage when elected officials cannot optimize their placement of public funds. Our interest in this legislation is not in advancing the interests of non-Kansas banks but rather to give boards of county commissioners additional options to invest county funds where it optimizes their return for their citizens and taxpayers.

In summary, the Kansas Association of Counties views this as an issue of local control. We believe the public interest is advanced by removing the current restriction for counties to designate non-Kansas banks as county depositories. Thank you for the opportunity to comment on this bill.

The Kansas Association of Counties, an instrumentality of member counties under K.S.A. 19-2690, provides legislative representation, educational and technical services and a wide range of informational services to its member counties. Inquiries concerning this testimony should be directed to Randy Allen or Judy Moler by calling (785) 272-2585.

6206 SW 9th Terrace
Topeka, KS 66615
785•272•2585
Fax 785•272•3585
email kac@ink.org

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Attachment 2

The City of
Overland
Park
KANSAS

City Hall • 8500 Santa Fe Drive
Overland Park, Kansas 66212
913/895-6000 • Fax 913/895-5009

January 30, 2001
TO: House Local Government Committee
Testimony in Support of House Bill No. 2086

Good afternoon. I am David Scott, Manager of Finance & Accounting for the City of Overland Park. I have worked for this City for thirteen years, and for the last ten years I have been managing the City's investments of idle funds.

Today our City's investment portfolio is approximately $70 million. During the year 2000, these investments generated $5.4 million dollars of interest income for the citizens of Overland Park. Thus, you can see interest income is a significant revenue source for our City, and if we had to raise this through property taxes our mill levy would have to go up 2.7 mills, which is a 36% increase.

In today's global economy, especially with the growth of e-commerce, the physical location of a company is no longer a critical factor for a customer looking to conduct business. No, today's customer is focused on:

- Pricing.
- the Quality of the product or service.
- and Availability and delivery of goods or service.

I feel that the current Kansas Investment laws create an artificial investment barrier that does not hold the best interest of the citizens, but instead holds the best interest of the local banks.

Overland Park **supports** House Bill No. 2086 because it:

Increases competition among financial institutions. This increase in competition will allow local governments to receive higher interest rates, resulting in increased interest income earnings. Thus, the need for higher property taxes will decrease.

Overland Park **supports** House Bill No. 2086 because it:

Provides an economic buffer to local governments during a slow-down in local economy. The U. S. economy does not always experience the same slow-down in all of its regions. In some regions, a financial institution's need for loan funds may drop off while other financial institutions outside that region still have steady loan demands. By allowing the financial institutions outside of Kansas to bid, local governments can benefit from others not affected by slow economic times.

Overland Park **supports** House Bill No. 2086 because it:

Creates an opportunity to increase the diversification among financial institutions holding local governments' funds. Diversification of financial institutions holding local governments' investments is good because it minimizes credit risks.

In conclusion, I feel that House Bill No. 2086 will eliminate the artificial investment barriers existing today and will allow for competitive investment markets to better serve the taxpayers of Kansas.

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Attachment 3

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TESTIMONY – HOUSE BILL 2086
DEPOSITORIES OF PUBLIC FUNDS

To: House Local Government Committee
Representative Gerry Ray, Chair

From: Charles A. Henry, Director of Revenue/Treasury
Unified Government of Wyandotte County/Kansas City, KS

Date: January 30, 2001

Dear Representative Ray and Committee Members:

I come before you to testify in favor of House Bill 2086.

In the Unified Government, we selected our primary depository bank through the issuance of a Request For Proposal. That primary bank clears all of our warrants, accepts all of our deposits, and invests our checking account balance overnight and over weekends. That process is not expected to be affected by this bill. In fact, it is unlikely that the Commission would allow our primary operating account be handled by any institution without a large presence in our County. However, this legislation offers an opportunity to other banks, forcing an increased level of competition for the business offered by the Unified Government.

The most important feature of this bill to the Unified Government is the expanded investment opportunities.

When our cash-flow model reflects an amount of cash available in excess of our immediate needs, we solicit bids for the funds. Our bid requests are sent to the eight institutions which have expressed interest in bidding on our idle funds which have offices in our County and a main office in the State of Kansas. We indicate the amount of money we want to invest and the date we would like it to mature. We ask the institution to bid either a Certificate of Deposit, a Repurchase Agreement, or a U.S. Treasury obligation. We indicate to each institution that they can bid on all or any part of the total amount to be invested. If no institution bids in excess of the Treasury rate, we look to the Kansas Municipal Investment Pool for an investment.

This bill would permit us to expand our bid list to at least three other institutions with offices in our County but with no Kansas Charter. Two of these three hold Missouri charters only. The other likely holds several state charters but is primarily based in North Carolina. These are institutions which serve our public, pay us property taxes, and offer checking accounts for our employees but with whom we can not invest our idle funds.

The bill would also permit us to expand our bid list to several institutions located across the river from us in Kansas City, Missouri. Whether we would choose to solicit bids from those institutions would require decisions by the Cash Management Committee and potentially the Unified Government Commissioners.

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The biggest challenge to this bill is from the banks that enjoy the advantage of limited competition at the expense of the taxpayers of the municipality. These banks contend that the lack of availability of low-cost government funds puts in jeopardy their ability to re-invest in the local community. It is our contention, that those funds are still available, if the institution is willing to pay market rates.

Our citizens/taxpayers expect those of us employed by the Unified Government to be professional stewards of the money entrusted to us, maximizing the value returned for the taxes collected. For us to maximize those tax dollars, and provide enhanced services to our citizens, we must be able to maximize our yield on safely invested dollars. This bill is a major step in that direction. This bill offers the Unified Government the chance to earn additional investment income at no cost to the taxpayer. Because the law and our policies remain unchanged regarding depository security, the taxpayers are not at risk.

For these reasons, I stand before you in support of House Bill 2086.

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Johnson County, Kansas• Office of the County Treasurer
Wm. E. O'Brien, County Treasurer

BEFORE THE COMMITTEE ON LOCAL GOVERNMENT

Tuesday, January 30, 2001

House Bill No. 2086

Testimony of Thomas Franzen
Chief Deputy County Treasurer, Johnson County

Madam Chair and Members of the Committee:

My name is Thomas Franzen, and I am representing the Johnson County Treasurer's Office. I am appearing in support of House Bill No. 2086.

As currently proposed, House Bill No. 2086, in effect, proposes to remove the requirement that any "municipal or quasi-municipal corporation" (governmental entity) utilize only depository financial institutions that have a Kansas state charter. The intent of this bill would be beneficial to taxpayers primarily because of the bill's impact on competition. By restricting depository financial institutions to only those with a Kansas state charter, the current environment limits competition between financial institutions, potentially keeping costs of banking services high and yields on cash balances low.

The financial services sector in general, and the banking industry in particular, have seen a dramatic increase in mergers and acquisitions in recent years. Conceivably, this continued trend could lead to a minimal number of depository financial institutions with Kansas state charters. Decreasing the pool of eligible depository financial institutions could lead to a deterioration of the competitive landscape between eligible institutions. Financial institutions compete primarily on cost and service. Without sufficient competition, cost increases could be more prevalent, while service levels could decline.

In certain geographical areas of the State, the number of eligible depository financial institutions may be limited. Acquisition by a national or regional banking organization without a Kansas state charter could force some governmental entities with limited choices to establish a new relationship with an eligible depository financial institution that is more costly, or less convenient, or both.

Current legislation limits choices regarding depository financial institutions. In light of the merger and acquisition activity within the financial services sector over the past decade, modifying the current legislation is a prudent step to allow governmental entities

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to conduct business at the lowest possible cost, thereby passing potential savings onto taxpayers in the form of a reduced mill levy.

Thank you for the opportunity to address this important issue before the committee. I would be pleased to answer any questions.

111 S.Cherry Street, Suite 1500 • Olathe, Kansas 66061-3471 • (913) 715-2600 • FAX (913) 791-5360

(6)

DEPARTMENT OF FINANCE AND ADMINISTRATION
300 West Ash Street • P. O. Box 736
Salina, Kansas 67402-0736
Rodney Franz, Director
Telephone (785) 826-7240 • FAX (785) 826-7244 • E-Mail rod.franz@salina.org

Date: January 30, 2001

To: Representative Gerry Ray, Chairman
House Local Government Committee

From: Rodney Franz, Director of Finance
City of Salina, Kansas

Re: HB 2086, Regarding Depositories for Public Funds and Investment of Public Funds

Representative Ray, Members of the Committee, thank you for the opportunity to provide testimony in support of House Bill 2086.

My name is Rod Franz. I am currently the Director of Finance for the City of Salina, Kansas, and currently am serving as the President of the Kansas Government Finance Officers Association (KSGFOA), with a membership of almost 200 professional finance officers from Counties, Cities, USD's and the State of Kansas. The KSGFOA Board has identified this issue as being important to address.

House Bill 2086 amends some provisions of K.S.A. 9-1401 et seq relating to public deposits and depositories, and K.S.A. 12-1675 et seq relating to investment of public funds. The primary thrust of the bill is to remove limitation that governmental entities may invest only in banks with a main office within that entity or within the State. It also removes the requirement that we can purchase certain types of investments (Treasury Securities, Municipal Investment Pool) only if the Banks do not offer the established "Investment rate".

We support HB 2086 for the following reasons:

1. It maintains the safety of public funds by continuing the requirements for collateralization and security of public deposits and investments, providing for third party custody of securities, continuing the delivery vs. payment method of purchasing securities, continuing the requirement that a municipalities interest in securities be perfected, and by maintaining the limitation on the types of investment securities that can be purchased to very conservative and safe investments. Deposits are permitted only at Banks that are Federally or State chartered.
2. It makes the two statutes consistent with one another. Currently, K.S.A. 9-1401 permits deposits in banks that do not have a main office in the state under certain

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circumstances. K.S.A. 12-1675 does not permit purchasing investments from such a bank under any circumstances.

3. It simplifies the process. Eliminating the "main office" requirement and the requirement that certain types of investments may only be made if the investment rate is not matched by an institution with a main office in the unit, County, State, in that order simplifies the process of evaluating bids as well as simplifies the language in the statute.

4. Diversification of the investment portfolio is a safety and liquidity feature. HB 2086 will allow us to diversify our portfolios with regard to institution and to investment type. The way the statute is currently written, if an institution with a "main office" within the locality meets the "investment rate" the portfolio will be comprised entirely of Certificates of Deposit. While these are safe investments, if adequately collateralized, both safety and liquidity will be better served with a diversification of investments to several institutions as well as including treasury notes and bills and municipal investment pool investments in the portfolio.

5. Finally, it enhances the market in several ways.
   A. We may or may not get a better rate with a more open market. We certainly will not get worse rates, and with a more open and unrestricted market, the taxpayer can certainly have more confidence that the best rate possible was obtained.
   B. The fact of the matter is that sometimes a particular bank or group of banks don't want our money. They simply sometimes don't have enough need for capital, don't want to or cannot provide the required collateral pledging, or may have other reasons. In those circumstances, it would certainly be beneficial to have a wider market available. What happens now is they don't meet the investment rate in their bid, or do not bid at all, and we place our money in the pool or buy treasury notes. This can result in a portfolio that is to heavily weighted towards those instruments.
   C. Conversely, under the current system, when the market for Certificates of Deposit is high because the Banks capital needs are high, it is impossible to legally choose to invest in the Pool or Treasuries in order to meet liquidity or diversification goals. HB 2086 addresses these issues.

As public agencies, our business is not primarily that of making money on money. However, as an adjunct to our primary mission of providing public services, we do hold public funds. It is incumbent upon us to be good stewards of those resources by insuring their safety, by insuring they are available to provide services when needed, and by providing a reasonable and competitive rate of return during the period that we do have custody of those funds.

HB 2086 enhances our ability to meet all three of those objectives.

Thank you.

Testimony of the City of Lenexa
in Support of House Bill No. 2086

Dennis J. Howard
Chief Financial Officer
City of Lenexa
12350 W 87th St Pkwy
Lenexa, KS 66215-2882
913-477-7544
dhoward@ci.lenexa.ks.us

Good morning. My name is Dennis Howard, Chief Financial Officer for the City of Lenexa. On behalf of the City, I would like to express our support for House Bill No. 2086.

Over the past several years, the City of Lenexa has experienced significant difficulty in complying with (or, more properly, *staying* in compliance with) the statutes governing designation of official depositories for both active and idle municipal funds. As the Committee is aware, both sets of statutes impose a preference in favor of in-state financial institutions. However, because of the high level of activity in bank mergers and acquisitions, it is nearly impossible to ensure that an in-state bank, "officially designated" as a depository will *remain* an in-state bank for any length of time.

The City of Lenexa, for example, designated an in-state bank as the depository for its active funds, but a few months later, the bank was purchased by an out-of-state bank. This automatically put the City out of compliance with the law through no fault of the City. We believe public officials and municipalities should be shielded from liability under such circumstances, and House Bill No. 2086, accomplishes that result.

Another problem is created by the fact that the current statutes pertaining to *active* municipal funds impose a preference in favor of any in-state institution that submits an "acceptable bid." Unfortunately, the statutes do not provide any guidance for interpreting the meaning of "acceptable bid." House Bill No. 2086 will give us the ability to better compete in today's financial markets.

In light of the many administrative and, potentially, legal problems created by the current statutes relating to designation of depositories, the City of Lenexa would strongly prefer that all locational restrictions be removed from the statutes.

I would be glad to answer any questions the Committee may have.

Fo11.0120010130hb2086

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CITY OF WICHITA

TESTIMONY

City of Wichita
Mike Taylor, Government Relations Director
455 N Main, Wichita, KS. 67202
Phone: 316.268.4351 Fax: 316.268.4519
Taylor_m@ci.wichita.ks.us

House Bill 2086
Public Funds and Banking Services

Delivered January 30, 2001
House Local Government Committee

The City of Wichita supports House Bill 2086. The bill will eliminate a special interest provision in Kansas law which forces local governments, including cities, counties and school districts, to deposit public funds only in so-called "hometown" banks which have a state charter.

Local governments should be allowed to use any federal or state chartered financial institutions which local officials determine offer the best value for the taxpayers they were elected to represent. The current restriction on local government is antiquated, anticompetitive, unreasonable and unworkable. It does not allow the most efficient use of tax dollars. In fact, in many cases, it mandates wasteful spending, requiring local governments to pay more and get less.

The current state law is a textbook example of powerful special interests at work. It guarantees that one small segment of the banking industry gets lucrative, near exclusive access to public funds at the expense of taxpayers. The current law prevents the City of Wichita from receiving bids from some of the largest banks in Kansas. Banks which can likely offer more services for less cost. The fact is, the City of Wichita has such large deposits and requires such sophisticated financial transactions, most of the so-called "hometown" or state chartered banks can't handle the business and don't want it. House Bill 2086 will allow the City of Wichita to be more effective and efficient with tax dollars. Meanwhile, smaller local governments, which don't require such complex services, could continue using so-called "hometown" banks if they choose.

It does not make sense that the Kansas Legislature would continue to prevent the most efficient use of tax dollars and in many cases, require wasteful spending. House Bill 2086 will allow public funds to be invested in the best and most effective way. It will expand the number of banks allowed to compete for public funds. We are convinced increased competition for public fund deposits and banking services will improve the type and array of services offered, lower the cost of those services and bring a better investment return for taxpayers. The current law which severely restricts which banks local governments can use, does not place the same restrictions on State government.

Managing public money involves a special trust and requires public officials to use caution, diligence and expertise to make sure those funds are invested in the public interest. That not only means making sure the funds are safe, but bring the best value and return to the taxpayer. House Bill 2086 will finally allow that to happen.

Answer.
8 Questions

TESTIMONY

City of Wichita
Carla Palmer, City Treasurer
455 N Main, Wichita, KS. 67202
Phone: 316.268.4444 Fax: 316.268.4656
Palmer_c@ci.wichita.ks.us

CITY OF WICHITA

House Bill 2086

Public Funds and Banking Services

Delivered January 30, 2001
House Local Government Committee

House Bill 2086 is a bill that provides competition to the banking industry for municipal deposits. It also provides municipalities the opportunity for enhanced services and increased interest earnings.

The Current Law
The current state statute requires municipalities to saturate local banks with municipal deposits before we can utilize other - more liquid - investment vehicles. Basically - municipalities are required to offer all deposits to the local banks first, then if the banks don't want the money, we are allowed to proceed with other investment alternatives.

The current statute limits municipalities from properly diversifying their investment portfolio, based on local banks need for funds.

The current statute allows municipalities to use primary dealers for repurchase agreements in the event no local bank is willing or able to do the investment. In actual operations, no primary dealer will undertake this investment because the statute requires them to deviate from their internal practices and deliver investment collateral to a local bank. Most primary dealers have contractual relationships with large financial institutions (typically in New York) where collateral can be transferred internally without the expense of wire transfer and delivery fees and numerous third party collateral and safekeeping agreements.

How the Current Statute Hurts Wichita
The requirement to deliver securities underlying repurchase agreements to a local financial institution significantly impacts the City's ability to use repurchase agreements.

For instance, an overnight repurchase agreement for $2 million dollars at 5% before fees would equate to 4.5% after fees.

Local banks have the right of first refusal on investment funds. This could have the effect of over-weighting a municipal investment portfolio with bank certificate of deposits. This is not a prudent investment strategy. A prudent investment portfolio limits risk by diversifying the portfolio by type of investment as well as the maturity structure and the issuers.

In the year 2000, the City of Wichita earned $15.4 million dollars in interest earnings and maintained an average portfolio size of $260 million dollars. The City's annual investment return for 2000 was 5.74%. For the City of Wichita, one basis point equals $26,000. The [illegible] annual spread

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..veen the Federal Reserve's historical interest rates for 6 month CD's and the State's require. Investment Rate for 6 month CD's is 49 basis points. Based on the maximum percentage of CD's authorized in the City of Wichita portfolio, the City could have increased its return by 10 basis points to 5.84% by simply enhancing competition and expanding the use of repurchase agreements. This equates to $260,000 the Wichita City Council could use to budget for City services.

This significant amount of money could fully fund six additional police officers or two youth recreation programs for a full year. This money belongs to the Wichita taxpayers.

This is not just about money; it's also about operational efficiencies…let me give you an example:

Recently, there was federal grant money available under CDBG to assist our citizens with their dream of owning their own home. The City was seeking a banking partner who would service individual mortgages and establish escrow accounts for pre-qualified individuals. The project required the financial institution to collect and account for monthly mortgage payments and provide some reporting. We estimated activity to be between 5 and 10 loans a year. Most of the financial institutions we spoke with were not interested in such a low-level of activity. The institution that would work with us used a third party mortgage service provider that did not meet the state statute of depositing funds locally. The law as it currently exists, severely limits our ability to offer this beneficial community service to our citizens.

How will House Bill 2086 benefit Wichita?
This legislation will allow the City to deposit monies and use the banking services of any federal or state chartered financial institution.

House Bill 2086 allows municipalities to diversify their investment portfolios based on prudent investment practices. This bill requires local banks to compete on a national scale for certificate of deposits.

House Bill 2086 allows collateral to be held in any federal or state chartered financial institution. This allows the City to enter into a contract with a New York Bank to hold collateral thus eliminating the cost of transferring securities locally. It also will expand the number of dealers willing to offer repurchase agreement services.

Many municipalities including Wichita have sophisticated treasury operations and investment programs. In today's age of technology, where we are expected to do more with less, a municipality the size of Wichita needs partners who specialize in municipal services. We need our banking partners to keep us abreast of trends and services that other cities use. Regional and National Banks have municipal clients our size and they have whole departments that specialize in municipal treasury services.

The City of Wichita spends approximately $130,000 annually on treasury services. It is difficult to attach a dollar value of savings in banking services if we utilized a non-Kansas chartered bank. The total dollars might not significantly change, but the services purchased with the dollars would elevate with the use of increased technology. This is likely the reason that the 1997 legislature removed the requirement for the State of Kansas to use a State chartered bank.

Our responses to expected Objections
As you listen to the testimony today, you may hear the following concerns from the banking industry:

Municipal deposits are at greater risk in banks outside Kansas.

?086 continues to require 100% collateral on all municipal deposits. The collateral requiren s ... AAA quality. The statute requiring evidence of ownership is not changing, nor is the requirement for securities to be delivered against payment.

Banks invest municipal deposits back in the community through housing and business loans and other necessary services throughout the community.

Nothing in the current statute requires banks to re-invest municipal deposits back in the community. Banks are in the business of making money. They will put the money to work where it will make them the most return. They are using the same investments that we are requesting. The truth is, banks are the middlemen in investment transactions at the expense of the taxpayers. A change in this statute will not make any changes in day to day banking or lending practices.

Community banks can't stay in business without municipal deposits.

Local officials, both elected and appointed are sensitive to community issues. The State should not attempt to mandate consciousness. Community leaders will take the necessary steps to encourage their local economy to prosper. This legislation does not require a change in the way business is currently conducted. In fact it allows local entities more flexibility when they choose to invest with a local bank because is eliminates the State's minimum investment rate.

Closing
The City of Wichita has good reason to continue our current banking relationships. We have established procedures and protocols not to mention the personal and professional relationships we have cultivated through the years. We believe that these partnerships are invaluable to our operations.

We believe in Community and working together to get the job done, just as the banks do; but we also believe in home rule, competition, fairness and free enterprise.

During 1999 the City issued a Request for Proposal for Banking services. Out of 23 local financial institutions, only three responded. Why? Because the needs of the City are complex. We require $18 million dollars in collateral; we write over 100,000 checks a year, we average $4 million dollars a week in deposits. We deal with check forgery, credit card fraud, change machine issues and over 15 locations depositing money on behalf of the City. City of Wichita finances are extensive and complex. We require a banking partner who brings technology, human resources and innovative ideas to the table.

Mandatory "hometown banking" is a thing of the past. The financial world today is global. We transact business over the Internet; we teleconference; we legitimately talk to machines. We have vast information systems at our fingertips, yet we still conduct our financial business the same as 1947, when this statute originated. It's time to update. It's time for a change.
House Bill 2086 encourages competition.
It provides municipalities the ability to prudently manage their own affairs without any additional risk.
It offers the potential to increase local revenues, decrease expenses and/or enhance services.

I ask for your support on House Bill 2086.

Thank you.

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Testimony before the House Local Government Committee
David W. Harris
Bank of America
January 30, 2001

Good afternoon members of the Local Government Committee. My name is David Harris, Senior Vice President with the Commercial Banking Group for Bank of America. My office is located in Wichita where I specialize in offering banking services to Municipalities throughout the state of Kansas. I appreciate the opportunity to appear before you today.

I am a Maize High Graduate of Maize, Kansas and a Graduate of Kansas State University, where I majored in Agriculture Economics. I have enjoyed a 15-year banking career, all of it in the state of Kansas.

I appear today in support of House Bill 2086 proposed by the League of Kansas Municipalities. House Bill 2086 would give Municipalities the "right" to choose deposit and investment services offered by non-state chartered financial institutions, such as Bank of America.

I would like to emphasize, this bill will not dictate where any Municipality must bank; it will only broaden the base of banking services from which Municipalities may choose. Based on my experience this change will result in a more competitive and efficient use of taxpayer dollars.

I would like to comment on Bank of America's commitment to offering "Value Added" products to Municipal Clients throughout the nation. In every state in which Bank of America operates we have a very strong client base of Municipal clients, <u>except for Kansas</u>.

Kansas is the only state in which we are unable to offer municipalities our complete product line. This is due to the anti-competitive nature of the existing law, which inhibits the ability of Municipalities to select from the deposit and investment products offered by Bank of America and other non-Kansas chartered financial institutions.

Bank of America has made a significant investment in resources to offer the very best product line of banking services to Municipalities throughout the nation. The partnerships and alliances we have formed with our municipal clients have proven to be beneficial for those clients.

Bank of America supports HB 2086 to create a level playing field to compete for municipal business in Kansas. We are not interested in obtaining an unfair advantage and passage of the bill won't create one.

We are certainly not the Financial Institution for everyone. We are only interested in having the opportunity to compete for the banking business of municipalities. The decision as to whom the various Municipal agencies will bank with remains with the governing body for that municipality.

The institution I work for is large and chartered out of state. However, that does not in anyway take away from the substantial commitment Bank of America has to the state of Kansas. For example:

Banking Centers	67
Communities	28 *
Bank employees	1,622 **
Automated Teller Machines	152
Non-Profit Organizations	153
Level of Financial Support to Non-Profits	$1,000,000+
Shareholders residing in Kansas	4,000+
Small Business Relationships (except KC)	3,400

Note: Largest SBA lender in the Wichita District from 10/1/99 to 9/30/00

* Covering all corners of the state from Pittsburgh to Liberal to Hays to Overland Park, and covering all points in between.

** Bank of America announced this past Friday that it will add 210 employees in Wichita, moving them from Atlanta, Georgia.

I mention these facts for one reason, I sense that when this issue is debated, there is the fear that "large" banks chartered out of state, pull resources from the state of Kansas.

I see no evidence of this. I have witnessed the evolution of Bank IV into Bank of America Kansas over the past five years. Through all of this, there has been no diminished level of commitment to the state of Kansas. Bank of America Kansas and its predecessor bank have 114 years of history here in Kansas, having been chartered in 1887. That's a significant commitment to the to State of Kansas, regardless of where we are currently chartered.

In summary, Bank of America is supportive of HB 2086, in an effort to see the establishment of a "Level" playing field regarding this Public Funds issue. Passage of the bill will result in a more competitive environment from which Municipalities may select their banking services.

I thank you once again for the opportunity to speak before you this afternoon. I would be glad to answer any questions.

(10)

FIRSTAR
Bank Without Boundaries

P.O. Box 178
Topeka, Kansas 66601-0178
785/291-1000

House Health & Human Services Committee
Testimony of Firstar
By Phil Ekstrom, President, Firstar—Topeka
Regarding: HB 2086, Investment of Public Funds
Tuesday, January 30, 2001

Chairwoman Ray and members of the committee. I speak on behalf of Firstar Bank corporately and our Kansas Charter. Firstar is a $75 billion company with a predominately upper Midwest presence. We have almost 500 Kansas employees. We continue to have a charter in Overland Park, Kansas which is due in large part so we can offer services to public fund customers.

Every company has to manage expenses if they are to survive. As a company, Firstar has duplicated expense by maintaining multiple charters versus collapsing into one charter. For business reasons, Firstar would like to consolidate charters but continue to offer services to public fund customers.

An argument used by some opponents has been the regional banks would accumulate deposits in Kansas and ship the deposits off to a distant metropolitan area while ignoring Kansas borrowers. <u>This argument doesn't hold water at Firstar.</u>

1. <u>Kansas Charter</u> (Kansas City, Topeka, Lawrence)

	@12/31/00	@12/31/99	Percentage Change
Loans	$1,502 billion	$1,372 billion	9.5%
Deposits	$1,977 billion	$2,040 billion	(3.0%)
Loan to Deposit Ratio	76%	67%	

2. <u>Topeka & Lawrence</u>

Loans	$ 467 million	$ 419 million	11.5%
Deposits	$ 466 million	$ 489 million	(4.7%)
Loan to Deposit Ratio	100%	86%	

Deposits have decreased due to bank and non-bank competition. This is a problem all Kansas banks face. Regardless, in spite of a shrinking deposit base, Firstar has aggressively increased our Kansas loan portfolio. <u>Our deposits fund Kansas based borrowers.</u>

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Competition is good and healthy. Competition keeps us sharp and aggressive. Not allowing banks with out of state charters to offer certain services to public fund customers would reduce interest received by the public entity due to reduced competition. Also, Firstar needs public funds to continue to fund Kansas loan growth. At 12/31/00, the Firstar Kansas charter had over $275 million in total public funds.

Firstar wants to continue to have the opportunity to do business with Kansas public fund customers regardless of where our charter is. This is good for Firstar, for our loan customers, for public entities, for Kansas.

Thank you for your consideration.

Phil Ekstrom
President

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Commerce Bank

1500 Wakarusa
Post Office Box 788
Lawrence, Kansas 66047
(785) 865-4770
FAX: (785) 865-4745

STATEMENT BEFORE THE LOCAL GOVERNMENT COMMITTEE
OF THE KANSAS HOUSE OF REPRESENTATIVES
BY DONALD A. JOHNSTON, CONSULTANT- INVESTMENT MANAGEMENT GROUP OF COMMERCE BANK N.A. AND A DIRECTOR OF COMMERCE BANK OF LAWRENCE, KANSAS

JANUARY 30, 2001

Chairwoman Ray and members of the committee. I speak on behalf of Commerce Bank N.A. of Kansas City, Missouri in support of this bill under consideration regarding the ability of local municipalities in Kansas to invest their funds with institutions chartered both within and without the State of Kansas. I speak also as a life-long Kansan.

Commerce Bank is certainly no stranger to the history and economic vitality of Kansas. Commerce Bank was founded in Kansas City in 1865, and has played a major role in the development of the metropolitan Kansas City marketplace over all the years, including being a very major partner in the outstanding development of northeast Kansas communities in particular. Commerce Bank currently operates a growing network of Kansas banking locations in Kansas City, Shawnee, Bonner Springs, Lenexa, Leawood, Overland Park, Olathe, Lawrence, Leavenworth, Lansing, Pittsburg, McCune, Columbus, Independence, Arkansas City, Winfield, Wichita, Derby, El Dorado, Hutchinson, Garden City, Manhattan, Lakin, and Hays.

Commerce Bank is a major regional bank with assets exceeding 11 billion dollars and over 300 branches in the states of Kansas, Missouri and Illinois. Our President, David Kemper defines our bank as a Super Community Bank, which means we pride ourselves in being positioned to deliver world-class, state-of-the-art technology and banking services to our customers while maintaining the kind of local control and Mid-western common sense which Kansas citizens demand. Our allegiance is here in this region, not to some gigantic corporate money center far remote from Kansas.

We now serve Kansas municipalities under current state law for over-night funds investing by utilizing our Kansas Charter bank in Wichita. This requires the dedication of a special window in each of our Kansas banks to address the banking needs of those local municipal officials. It further complicates severely the operational handling and investment management of those funds. If the proposed legislation were approved, Commerce Bank would be free to utilize its system-wide array of banking and investment tools to the fullest advantage for our municipal customers. In short, Commerce Bank would be able to bid for those local funds in a much more competitive manner which can be nothing but good news for Kansas communities. There is great cost to our bank to bid under the current law, The proposed law would significantly reduce that cost and allow your constituent municipalities to reap the benefit.

I cannot over-stress how committed Commerce Bank is to the State of Kansas. We certainly have a very large employee base in our various Kansas banks. Ever growing numbers of our Kansas City, Missouri bank employees live in Kansas and pay taxes there. Our officers and employees are deeply involved participants in the community life of their individual Kansas towns and cities, and each of those banks has a local Board of Directors made up of long-time business and professional leaders. Our local banks give generously to local charities, educational, and service organizations. In addition, The William T. Kemper Foundation, of which Commerce Bank NA is Trustee, is proud to have contributed large sums over the years to fund many local Kansas projects in the fields of health, human services, education, the arts, and civic endeavor.

We want to do business with Kansas municipalities and are eager to compete agressively for it. It is the hope of Commerce Bank that this proposed legislation will become the law of the State so that our bank can serve your municipalities with all of our unbridled ability in technology and in human skill and dedication for the benefit of Kansans.

KANSAS ASSOCIATION OF SCHOOL BOARDS
1420 SW Arrowhead Road • Topeka, Kansas 66604-4024
785-273-3600

TESTIMONY ON HOUSE BILL 2086
BEFORE THE COMMITTEE ON LOCAL GOVERNMENT

Norman D. Wilks, Attorney
Kansas Association of School Boards
January 30, 2001

Madam Chair and Members of the Committee, we appreciate the opportunity to appear before you on behalf of the member boards of the Kansas Association of School Boards to express our support for the adoption of HB 2086. USD No. 259, Wichita, KS joins us in support of this legislation.

The primary change included in HB 2086 is to remove geographical barriers that limit the ability of school districts to select their financial institutions based on sound business principles. School districts will be able to utilize any financial institution that is incorporated under the laws of the State of Kansas or organized under the laws of the United States. In some cases this means local school districts can now deposit their funds and use the financial institution in their local community even though there is not a main office located within the school district.

The change proposed by HB 2086 has long been supported by our legislative policies as approved by the member school districts. Our current legislative policy provides "district officials should be allowed invest district funds in time deposits, certificates of deposit or other authorized investment instruments in any bank or savings and loan institution authorized to operate in Kansas, or any direct obligations of the United States Government, such as treasury bills or notes. The board may negotiate rates of return for investments."

The proposed change recognizes the real changes that have occurred in financial institutions and still provides appropriate security for the return of school district funds. Security, service, convenience, income or return of investment is not improved simply because the financial institution maintains a main office in this state. If the financial institution is incorporated under the laws of the State of Kansas or organized under the laws of the United States, the financial institution has the ability to do business in the State of Kansas. The location of a main office in this state or a branch office in the local district may or may not have any impact on the financial institutions ability to provide quality services and secure deposits needed by the school district.

We support the changes included in HB 2086 for the following reasons:

1. Security of school district funds is maintained.
2. It removes outdated geographical barriers.
3. Provides an opportunity to increase investment income.
4. Allows a school district and financial institution to make a business decision based on mutual agreement and benefit, not the location of the "main office."
5. Recognizes the real changes in financial institutions because of mergers.
6. Gives local school districts greater flexibility in obtaining desired financial service.

For these and other reasons we urge your support and passage of HB 2086. Thank you for your attention to this matter and I am happy to respond to any questions.

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GOVERNMENT RELATIONS

Sedgwick County Courthouse
525 N. Main, Suite 365
Wichita, KS 67203
Phone: (316) 383-7552
Fax: (316) 383-7946

Michael D. Pepoon
Director

TESTIMONY ON H.B. 2086
House Local Government Committee
By Michael D. Pepoon, Director of Government Relations
January 30, 2001

Honorable Chair Gerry Ray and members of the committee. Please allow me to submit written testimony in support of House Bill 2086 on behalf of Sedgwick County. This legislation would give cities and counties the option of using a bank, which is not chartered locally, or in effect does not have its "main office" in the state of Kansas, for investments and other banking services. The effect of this legislation would give cities and counties more options to take care of their banking needs and create an environment of more competition from such banks for these services.

Sedgwick County's Chief Financial Officer, Chris Chronis, is out of town and could not be here to testify in support of this bill. According to Mr. Chronis, there are only four banks in Sedgwick County capable of handling Sedgwick County's banking services. This is due in part because of the large amount of money that a banking institution must pledge as collateral to protect the County's funds. On a daily basis the County will have between ten to fifteen million dollars go through our bank. There are four times a year when such amounts are in the range of one hundred million dollars. Because of this, one such bank has chosen not to handle the County's services. Another bank already provides these services for the City of Wichita and U.S.D. 259, and as such, will not bid for our services. This leaves only two local banks competing for our banking services. Sedgwick County is paying approximately $150,000.00 per year for its checking, lockbox, wire and other banking services. This lack of competition creates an environment whereby Sedgwick County is paying more and receiving less than it might receive if there were more competition.

Nothing in this bill prevents a city or county from choosing a "local" bank for their banking services or investment options. But the positive effect of this legislation for Sedgwick County is to create an environment of competition among banks and to give the taxpayers of our county better service for less money.

For the above stated reasons Sedgwick County strongly supports H.B. 2086.

(14)

City of Olathe

MEMORANDUM

TO: Members of the House Local Government Committee

FROM: Donald R. Seifert, Policy Development Leader

SUBJECT: **House Bill 2086**; Depositories for Public Funds

DATE: January 30, 2001

On behalf of the city of Olathe, thank you for the opportunity to appear today to add support for this bill. HB 2086 would authorize cities to designate any federal or state chartered financial institution as a depository for city funds. Under current law, local governments are authorized to deposit funds only in Kansas chartered banks with branches in the local community. This requirement limits the number of otherwise qualified banks eligible to provide banking services and act as depositories for public funds.

The city of Olathe recognizes that efficient cash management is an integral component of effective financial management. The city council has adopted an investment policy that governs the investment of idle funds until they are needed for the city's operations. At any point in time, the city maintains an investment portfolio of $80-90 million. The city's investment policy has been approved by the Pooled Money Investment Board (PMIB) for expanded investment authority under K.S.A. 12-1677b.

The city believes this bill is good public policy for several reasons:

1. Elimination of the state charter requirement will allow more competition for public funds. The city periodically requests proposals from financial institutions for both its banking services and investments. Under current law, response to proposals is restricted by location of bank charter and branch geography. More competition should enhance service and encourage more competitive rates when taking deposits from units of local government. This benefits the local taxpayers.

2. The bill will not compromise safety of public funds. No changes are proposed in allowable investments or the required security for those investments.

3. This bill reflects the current banking industry environment. Many communities simply do not have a Kansas chartered bank within their boundaries, but may have a number of federally chartered institutions competing and providing services to private, but not public customers.

Thank you for the opportunity to support HB 2086. The city urges the committee to recommend this bill favorably.

(15)

Community Bankers Association of Kansas

Directed By The Members We Serve

January 30, 2001

House Local Government Committee

Thank you for the opportunity to testify on House Bill 2086. Rather than testify on behalf of our association, I would like to introduce some of our members, who would like to testify. First, some information about community bankers and the business this bill would impact.

The Community Bankers Association of Kansas consists of locally owned banks, many of which are in rural communities in Kansas. In fact, more than 40% of our member banks are located in towns with populations of 1,000 or less. Over the last decade, in particular, our members have experienced a steady erosion of deposits. You may ask what that means. In brief, if your local bank doesn't have money available, through core deposits or otherwise, he or she doesn't have funds to lend out to farm, business or individual customers. This bill would create another drain on those deposits, further weakening the ability of our members to satisfy the capital needs of these local communities. I enclose some statistics from the Federal Deposit Insurance Corporation and the Federal Reserve Bank of Kansas City that quantify those facts for you. When you look at these numbers, it is true that public funds on deposit in most local community banks are not the largest category of deposits. However, it is just another incremental loss that, together with other pressures on capital, tightens up capital availability for rural customers.

With the Chair's indulgence, I would like to introduce CBA members who are here to testify.

Bob Kennedy
Executive Director

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1/30/01
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2942-B SW Wanamaker Drive, Suite 2A • Topeka, Kansas 66614-4186 • Phone (785) 271-1404 • FAX (785) 271-1508 • E-mail: info@cbak.org

Erosion of capital for local communities

	2000 *	1999 *	Increase/decrease
Number of FDIC insured banks	375	391	- 3.3%
Total assets	$ 36.6 billion	$ 33.9 billion	+ 8 %
Total deposits*	$ 38.5 billion	$ 38.8 billion	- 1%
Total loans/leases	$ 23.4 billion	$ 21.3 billion	- 9.9%
Loans to agricultural customers	$ 2.43 billion	$ 2.44 billion	- .4%
Loans to commercial customers	$ 4.83 billion	$ 4.25 billion	+ 13.7%
Loans to individuals	$ 3.45 billion	$ 3.28 billion	+ 5.2%
Loan/Deposit ratio	78.3 %	75.3%	+ 3%

www.fdic.gov - Statistics on Banking, Third Quarter 2000 vs Third Quarter 1999
* FDIC/OTS Summary of Deposits

Agricultural Credit Conditions

	1998	2000	Change
Loan to Deposit ratio	67.3%	68.8%	+ 1.5%
Loan fund availability (index)	104	87	- 16%
Farm Commodity Price Index (1980 = 100)	86.5	98.5	+ 12%

Federal Reserve Bank of Kansas, Center for the Study of Rural America, Survey of Agricultural Credit Conditions

Representative Community Bank	
Total Assets	$ 31.6 million
Total deposits	$ 28.3 million
• Individuals and companies	$ 25.6 million
• State and local government	$ 2.6 million
• Other	$ 100,000
Loans	$ 22.2 million

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House Local Government Committee
House Bill 2086

January 30,2001

D. Max Fuller
President and Chairman
The Stockgrowers State Bank
Maple Hill, Ks. 66507

Chairman
Community Bankers Association of Kansas
2942-B SW Wanamaker Drive, Suite 2A
Topeka KS 66614-4186

My name is Max Fuller and I am President of The Stockgrowers State Bank, Maple Hill, located about 20 miles West of Topeka. The Bank was established in 1906 and I have been President for the last 20 years. The Bank is about 24 million in total assets, 17 million in deposits and 14 million in loans or a loan to deposit ratio of 80%.

($ 000)

	12/31/95	12/31/00
Core Deposits	11,752	14,033
Large Deposits		
(other than idle funds)	1,117	2,489
(idle funds)	150	1,100
Loans	9,789	14,048
Ratio:		
Loans / Core Deposits	83%	100%
Large Deposits / Core Deposits	11%	26%
State Idle Funds / Large Deposits	12%	31%

With the decline in profitability in Agriculture it is getting more difficult each year for my Bank to attract sufficient deposits to fund our loan demand. The State Idle Funds are an important source of funds for my Bank and I am convince it is an important source for most Community Banks in Kansas. My plea to the committee is that HB 2086 be amended to leave the law in regard to Idle Funds in its present form.

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Questions?

Thank you for your consideration.

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Kansas Bankers Association

800 SW Jackson, Suite 1500
Topeka, KS 66612
785-232-3444 Fax - 785-232-3484 kbacs@ink.org

1-30-01

To: House Local Government Committee
From: Chuck Stones, Senior Vice President

Re: HB 2086

Madam Chair and Members of the Committee:

The Kansas Bankers Association appreciates the opportunity to appear before you regarding HB 2086.

KANSAS TAXPAYERS MONEY SHOULD STAY IN KANSAS FOR THE BENEFIT OF THE TAXPAYERS.

- **IT IS NOT THE LOCAL UNIT OF GOVERNMENTS' MONEY.**

If local units are going to hoard taxpayer money, it should, at least, be used to the benefit of the people in the taxing unit and the State.

Kansas is definitely a "host" state when it comes to interstate banking and branching. There are 11 out of state banks with 196 branches in Kansas, while there are 4 Kansas banks with about 15 branches in other states.

It is very evident that Kansas is mere acting as a deposit collecting area for some of the large multi-state banking operations. If more deposits are needed to fund activity in other states, they merely increase rates to collect the needed funding. The same would be true in the case of public funds. Kansas's taxpayers money would be used to fund projects in other states.

- **IT IS NOT ABOUT COMPETITION.**

In the last 15 years the number of banks has declined from a high of 628 to 372. In 1986 out of town branching was first allowed. There are now 178 Kansas banks with branches in other towns with a total of 423 out of town locations. In other words, there is more competition now than there was before.

18 banks have decided to put branches in Johnson County. The 21 banks chartered in Johnson County are already competing with them.

HOUSE LOCAL GOVERNMENT
1/30/01
Attachment 17

- **THERE IS NOT A NEED FOR THIS LEGISLATION.**

We have made every effort to be amenable to the concerns of the public units of government.

When the concern was expressed that banks were not bidding at all or not bidding a high enough rate for the money that local taxpayers had paid to the local unit, we helped design the Municipal Investment Pool. A bank must now bid a minimum rate, called the "Investment rate", or the local unit has the option to then place their money in the MIP.

When the concern was raised that some banks simply did not have the technology or the capacity available to handle some cities active accounts, we were willing to insert the word "acceptable" in the statute dealing with bids from banks with charters in Kansas. The word "acceptable" was purposefully left undefined in order give the local units maximum flexibility under the law.

We have not heard a valid reason to make this change. All the reasons cited are ***convenience*** factors for the local units. None address the issue of Kansas taxpayer dollars remaining in Kansas.

- **PUBLIC FUNDS ARE ONE OF THE VERY FEW REASONS THAT AN OUT-OF-STATE BANK WOULD KEEP A CHARTER IN KANSAS.**

There are currently 3 major out-of-state banks that have decided to maintain a charter in Kansas in order to qualify to hold public funds. Those 3 banks combined represent 17% of the total deposits in Kansas. Added to the current 18% of deposits of out-of-state branches, that would be a total of 35% of the total deposits in Kansas held in branches of out-of-state banks.

- **MANY KANSAS BANKS DEPEND ON LOCAL PUBLIC FUNDS AS A STABLE BASE OF DEPOSITS IN ORDER TO MEET THE NEEDS OF THEIR COMMUNITIES.**

Deposit growth in Kansas banks has been relatively flat. A lot of the growth in bank deposits has been because of conversions and purchases of S&L branches. We are seeing a "funding concern" in many rural areas of Kansas. As the population base ages and declines many Kansas banks find it difficult to sustain a stable deposit base. A bank in western Kansas did an internal study recently. They found that:

- **79%** of their core deposits were held by people 60 years of age or older
- The inheritors of **62%** of that money were not in their community
- The result will be a **51%** decline in the banks deposit base

An examination *of "The Governor's Economic and Demographic Report – 2000-2001"* shows the same scenario can likely be told throughout rural Kansas, and in many cases is already true in some very small rural communities. Kansas is above the national average for population over the age of 65 and 85. The percentage of people over the age of 65 makes up over 20% of the population in 42 counties. In addition, 38 Kansas counties are projected to have less population in 10 years than they currently have.

- **THIS IS NOT IN THE BEST ECONOMIC INTERESTS OF KANSAS**

Kansas spends millions each year on economic development in order to attract capital. Yet this bill opens the spigot and allows Kansas tax dollars to flow freely out of the state. For over 65 years we have had a sound policy of requiring that local public funds be invested locally if at all possible. Are we going to abandon this sound and logical policy just to please a small number of out of state banks, whose primary interests are merely deposit gathering, or for the convenience of a few cities.

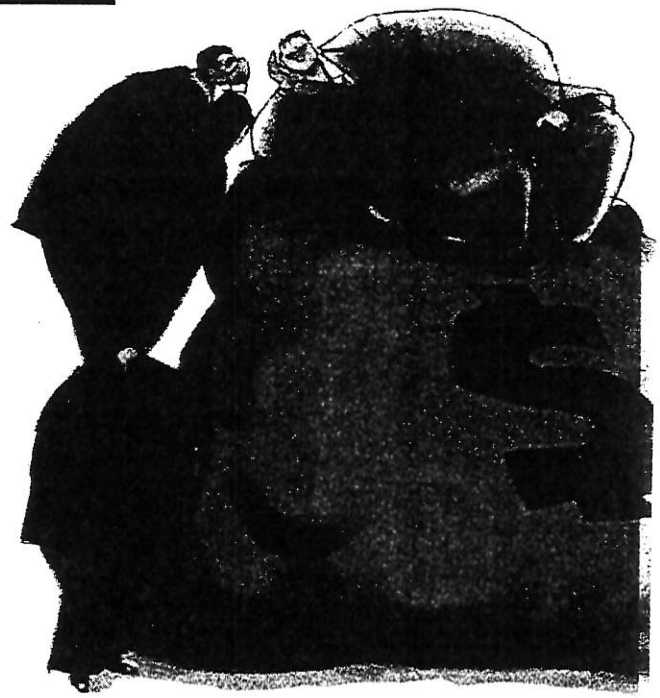
Where is the logic in putting forth all the effort on economic development and then casually allowing out-of-state institutions to raid Kansas capital?

The multiplier effect has a dramatic effect when you look at public funds on deposit with Kansas banks.

- **$2.8 billion** of public funds on deposit at Kansas banks
- **68%** loan to deposit ratio
- multiplier effect of 4 = **$7.6 billion** economic benefit
- **$456 million** benefit to the state if economic growth is taxed at 6%

Looking at the benefits, local units of governments seem very short sighted in promoting this proposal. How much of this benefit is the state willing to lose?

The search for funding



Regulators, bankers, and home loan bank leaders debate the risks of nontraditional funding

In the movie "Cool Hand Luke," the top guard summed up a troublesome situation with the immortal line: "What we have here is a failure to communicate."

One could say that a similar problem has existed, until recently, among three key groups in American finance:

* Community bankers who for some time have needed to supplement dwindling local core deposits with alternative, nontraditional, often "wholesale," funding.

* The Federal Home Loan Banks, which have filled much of that gap, and will presumably do more of that, now that small business and farm loans can also be used as collateral for home loan bank advances.

* The three federal banking regulators, who clearly have a strong interest, if not outright concerns, over liquidity.

In the last few months there has been an effort among elements of all three groups to have some meeting of the minds. This has taken place in tri-partite private meetings requested by ABA and others, and in other forums. But this is a gradual process, as communication often is, and it is fair to say that community banks can expect their funding techniques to continue to be a regulatory issue—even as the apparently slowing economy may reduce the urgency of the situation for a time.

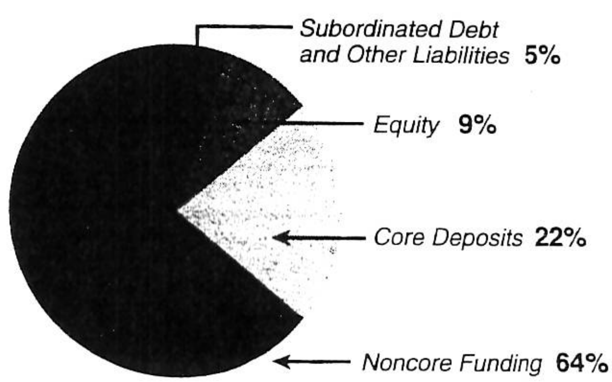
The stakes involved here are sobering. In the absence of substantial reform of deposit insurance rules, many bankers think the bulk of their traditional core deposits are gone for good. And the specter of trouble for the Bank Insurance Fund, due to the high volume of home loan bank secured advances, has even been raised.

Whispers and worries

The issue reflects a confluence of events, among them a record-busting economic boom and the ongoing shift in consumer appetites for investment risk that first took root in the late 1970s. Over the last five years, while core deposits grew by about 3%, assets grew by about 7%, according to FDIC figures for all insured institutions.

What's more, loan-to-deposit ratios' range of "normalcy" shifted drastically. During the early-to-mid 1990s, the loan-to-deposit ratio hit 74% and that was considered high, according to FDIC analyst Allen Puwalski; nowadays, the industry is in the mid-90% range and some banks have broken the 100% mark.

Most of $2 Trillion of Asset Growth since 1995 Was Funded with Noncore Funds



Source: Bank and Thrift Call Reports, June 2000 and June 1995

These economic shifts have not been without their ripple effects.

As evidence of this, Mark S. Schmidt, associate division director-policy, FDIC Division of Supervision, notes that the last six months or so have seen a deterioration in the "L" (liquidity) component of the CAMELS rating. After a stable 1998 and 1999, Schmidt says, the agency began to see an increase in the proportion of insured institu-

By Steve Cocheo, executive editor

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tions that had a "3" rating. The top rating is "1," and Schmidt explains that a "3" indicates that the bank is a marginal performer, in terms of liquidity—"not bad, but could be better," he says.

Schmidt cautions against making too much of this fact. "We're still talking about a small percentage of banks," he explains. Institutions with liquidity ratings of 3, 4, or 5, he says, represented 3% of the industry over the last few years, but now represent about 5%. (FDIC officials insist that simply having a high loan-to-deposit ratio doesn't earn a bank an inferior "L" rating—the bank would have to demonstrate that it isn't properly matching liability and asset maturities, for instance.)

Nevertheless, this and similar indicators have caught regulators' attention. Indeed, a little while back, a rumor was floating around that federal regulators planned to start conducting special liquidity visitations or examinations.

The rumor, as best as we can determine, turned out to be false. Each federal banking regulator contacted insisted there was no need for such special visits—it's an exam basic.

Yet there was a story there: To varying degrees, the federal regulators have concerns about community banks' use of nontraditional, wholesale funding sources. They are expecting banks to be able to demonstrate that they have a rhyme and reason for the way they are funding their operations, particularly if they've gone beyond core funding to support portfolio growth. More than three-quarters of the nation's commercial banks now belong to the Federal Home Loan Bank System, for instance.

Some of the Washington headquarters types—most notably at the Comptroller's Office—put more stress on the issue than others, but anecdotal reports from bankers indicate that field examiners from

FUNDING *continued on p.9*

all three agencies have heightened their scrutiny of funding.

Typical comments come from two bankers about Federal Reserve examiners. "We just had a Fed exam and the examiners clearly favored traditional funding sources over nontraditional sources," says the CEO of a small Texas bank.

Says a Virginia community bank CEO: "We haven't used Federal Home Loan Bank funding in recent years, but I still had to spend about an hour justifying why I even had a credit line with our home loan bank for my Fed examiner."

Such reports don't come as a surprise to banker Earl McVicker, president of Central Bank & Trust, Hutchinson, Kan., and co-chairman of the recently formed ABA Funding and Liquidity Steering Group (ABA BJ, Dec. 2000, p.10). McVicker is involved as an investor or officer with a half-dozen other community banks—with both national and state charters.

*

"A couple of years ago, I had an examiner tell me, 'Just stop making loans'," if funding was scarce, says McVicker.

McVicker acknowledges that the examiner corps seems a bit more liberal-minded now, but says that initial discussions among members of the ABA steering group indicate that there is a great deal of questioning going on by examiners. He recalls how one banker was asked—as if he could control it—what he would do if the home loan bank system lost its GSE (government sponsored enterprise) status.

Something that particularly troubles McVicker: reports that attitudes can vary from one regulatory district to another regarding nontraditional funding. One goal he hopes the steering group can achieve is greater consistency.

Shadows of the '80s

There are bankers doing business today who were still in school during the thrift crisis of the 1980s, but the regulatory agencies look at funding issues from a historical perspective that includes that debacle. The basic fault of the early thrift troubles—borrowing short to fund long-term mortgages—is very much on their minds.

"The funding source itself isn't so much the problem, but what you are doing with it," says John M. Lane, associate director for operations in FDIC's Division of Supervision. In addition, he cautions, "remember, you are locking up a sizeable part of your asset base for collateral purposes" when using secured FHLB advances.

Even if a bank is appropriately match-funding—using

FUNDING *continued on page 61*

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AMERICAN BANKER®

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Rural Banks Feeling Shaky as Population Erodes

◆ By LAURA PAVLENKO LUTTON

Worn out after a year of unpredictable weather and low crop prices, six young men who farm together near Finley, N.D., plan to call it quits after the fall harvest and move their families to the city.

It's a story that has become all too familiar to Roger Monson, president of Finley's only bank.

Since 1980 more than one-quarter of the residents in Finley and its surrounding county have moved away, according to the U.S. Census Bureau. That has left $29 million-asset Citizens State Bank struggling to find deposits and make loans.

"We're looking to see how we can remain viable in a shrinking market," Mr. Monson said.

Though most urban community banks battle to keep customers from switching to a competitor, many rural banks simply want to keep their customers in town. According to a new study by the Federal Reserve Bank of Minneapolis, one-quarter of the district's rural banks cited an aging or declining local population as their leading concern.

Of the five states in the Minneapolis

See page 6

Troubled Times

Rural banks surveyed in five midwestern states

41% described local market conditions as fair or poor

50% are in counties that lost population from 1990 to 1997

25% cited aging or declining population as the No. 1 market challenge

Source: Federal Reserve Bank of Minneapolis

Tomorrow: Mortgage Technology, a Special Supplement

Farm Banks Feel the Pinch As Rural Populations Shrink

Continued from page 1

Fed region, only Montana had an increase in rural population from 1980 to 1990, according to the U.S. Census Bureau.

And though population is shrinking in rural regions nationwide, the trend is most pronounced in the 12 midwestern states, which had a 2.6% decline in rural population during the 1980s.

North Dakota reported a 10.7% population decline — largest in the Midwest, census figures show.

And it's only getting worse. Department of Agriculture studies say that most rural counties in the Midwest have lost residents since the last census and will continue to do so.

That spells more trouble for bankers who are already facing the challenges of low farm prices and young customers who would rather invest their savings in the stock market than in certificates of deposit.

"This is a chronic problem that bankers are wrestling with every day," said George G. Beattie, executive vice president of the Nebraska Bankers Association. "Their existence depends on how well they deal with it."

Keith Leggett, an economist at the American Bankers Association, said rural communities often lose residents because there are no jobs to keep them there.

Many small towns rely on the farm sector as a major employer, so when farmers quit because of low prices, bad weather, or old age, new businesses often do not spring up to replace the old, Mr. Leggett said.

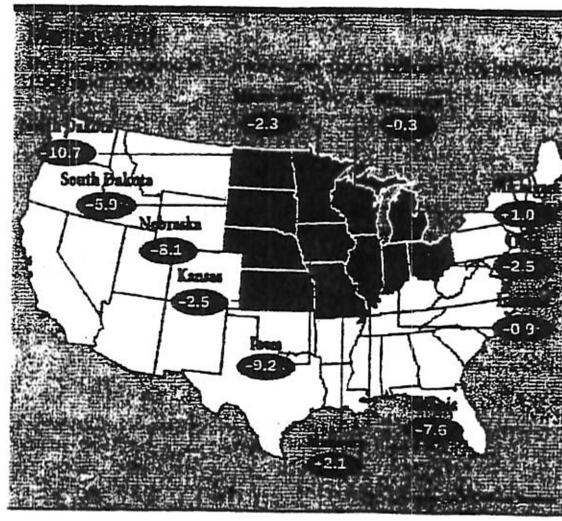
"A declining population is usually linked with a decline in the economic condition," he said.

Bankers feel the impact of a declining population when elderly customers die.

The customers' children — many of whom have moved to the city — typically withdraw their parents' deposits and often invest them in the stock market.

Then the banks must turn to more expensive sources of funding, such as brokered deposits or seasonal farm loans from the Federal Reserve, to stay liquid and meet loan demand.

Such is the case at Ravenna (Neb.) Bank, where 75% of the bank's deposits are held by senior citizens.



Dale E. Pohlmann, president and chief executive officer, said that as those deposits are willed to the younger generation, he buys brokered certificates of deposit and borrows from correspondent banks to keep the $47 million-asset bank's loan-to-deposit ratio at 80%.

Mr. Pohlmann said Ravenna plans to join the Federal Home Loan Bank System to expand its funding sources.

The squeeze comes when elderly customers die and the heirs remove inherited deposits.

Many agricultural banks had been barred from FHLB membership because they do not make enough mortgage loans to qualify. But a change adopted this summer lets banks pledge agricultural real estate loans as collateral for Home Loan Bank advances.

Aside from replacing deposits with purchased funds, bankers say they are looking for long-term solutions to reverse the population decline.

Economic development projects, which many community banks support, have helped in some cases.

Janesville, Minn., which has 2,000 residents, has stemmed its population decline by building a housing development with the support of local government.

The new homes, along with a new golf course, are giving young families a reason to call Janesville home, said Michael Finley, president of $38 million-asset Janesville State Bank.

Though Mr. Finley said he was encouraged by the growth, he noted that younger customers are harder to attract.

"Younger people aren't as willing to put their money into the bank," he said. "The bank has to learn how to draw them in."

Some rural community banks, such as Peoples State Bank in Mazomanie, Wis., are drawing more business from a younger customer base by setting up investment centers that give financial planning advice or by investing in technology to allow Internet banking.

But Mr. Beattie of the Nebraska Bankers Association said he believes the population trend toward aging and shrinking will continue.

Ultimately, small community banks may need to join forces to survive.

Mr. Monson said he would consider merging Citizens State with a bank of similar size so the pair could save on overhead and operating expenses.

Such a survival technique could become common, he predicted.

"A majority of these community banks are not just rolling over and dying," he said. "It's just another challenge." ◇

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AMERICAN BANKER

Community Banking

Small Banks Face Crisis as Deposits Drain Away

By Laura Pavlenko Lutton

Community banks are finding it increasingly tough to meet deposit and withdrawal demands as customers shift their deposits into higher-yielding investments like mutual funds.

"I think it could become a crisis," said C. William Landefeld, president of Citizens Savings Bank in Bloomington, Ill., and chairman of America's Community Bankers. "It's one of our biggest concerns."

Over the last three years, loans at banks with assets between $100 million and $1 billion have grown nearly 11% while deposits only increased 3.27%, according to the Federal Deposit Insurance Corp.

At June 30, loans at these banks averaged 74% of deposits -- an all-time high.

"We're clearly seeing some community banks struggle with liquidity," said Keith Leggett, an economist at the American Bankers Association. Loan-to-deposit ratios above 70% force these institutions to seek alternative sources of funds to meet loan demand -- a move that can squeeze profit margins.

"Banks may give up liquidity to meet loan demand and that raises a safety question," he added.

While deposits are leaving banks of all sizes, the problem is worst at small banks because they have fewer funding sources.

"The big banks can issue debt securities, but we can't really do that," said Arthur C. Johnson, president of United Bank of Michigan, a $165 million-asset bank in Grand Rapids. "Smaller banks don't have the same access to the capital markets."

Many of these banks also are in towns with dwindling populations or slumping economies.

Dennis Utter, president of $45 million-asset Adams County Bank, said it's difficult to keep deposits in the bank's hometown of Kenesaw, Neb. Baby boomers have moved much of their savings to alternative investments, and younger depositors are even tougher to attract, he said.

"When an old, loyal customer passes away, those funds don't stay in Adams County

Bank," he said. "The heirs don't live here anymore."

To increase liquidity, community bankers are turning to the Federal Home Loan Bank System, seeking out deposit brokers, nudging up interest rates, or selling off assets.

The 12 Federal Home Loan banks, which lend money to member institutions, are a popular source of funds for community banks nationwide. Membership in the system has doubled in the last six years to roughly 6,300, and through August total loans were up 10.3%, to $177.8 billion.

Mr. Johnson said United Bank of Michigan has borrowed $5 million from the Federal Home Loan Bank of Indianapolis to fund loan growth.

But the Federal Home Loan Bank System is not the answer for all community banks. Membership is limited to banks and thrifts with mortgages making up at least 10% of their total loan portfolios. What's more, only mortgage loans may be used as collateral, further limiting what some institutions may borrow.

William L. McQuillan, president of City National Bank in Greely, Neb., said his bank went out and bought enough mortgages to meet the 10% test so it could start borrowing. "We couldn't continue to go out in the local market and pay up for deposits," he said.

The membership and collateral requirements soon may be relaxed through rule changes and pending legislation.

For example, banks may be able to reclassify some agricultural loans as mortgages under a proposed rule, and pending legislation would waive the 10% mortgage rule for banks with assets under $500 million -- making 800 more banks eligible for membership.

In the meantime, banks may buy deposits from brokers. Mr. Utter said he buys about $5 million of deposits to get Adams County Bank through the peak agricultural lending season of April through October.

"Brokered deposits used to be really frowned upon by regulators, but we're not funding long-term investments," he said.

Banks also sell older loans in their portfolios, branches, or other investments to boost liquidity.

Gary Scott, president of Cheatam State Bank in Kingston Springs, Tenn., said his bank occasionally bundles 15- to 20-year mortgages and then sells them to raise cash.

Citizens Savings Bank recently sold one of its under-performing branches to bring in new funds. The bank sacrificed the branch's $7 million of deposits, but Citizens was able to use cash from the sale to pay off some Federal Home Loan bank advances, Mr. Landefeld said.

First Dakota National Bank in Yankton, S.D., has sold off municipal bond securities in recent years to increase its loan capacity, according to its president, James Ahrendt.

Lew Stone, president of Goleta (Calif.) National Bank, said his bank is using the Internet to solve liquidity problems.

Goleta sells certificates of deposit through an electronic bulletin board, raising and lowering the rates depending on how much money the bank needs. "We could raise $10 million overnight if we had to," Mr. Stone said.

Industry experts say they expect the current trend of declining deposit growth and increasing loan demand to continue.

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"I don't see any real relief for community banks," said Charles N. Cranmer, head of equity research at M.A. Schapiro & Co. in New York. "You've got a banking population that's been educated that they can do better things with their money than put it in a bank."

AMERICAN BANKER

WASHINGTON

Tuesday, March 9, 1999

Funding Crunch Looms, Rural Banks Warned

By Jaret Seiberg

ARLINGTON, Va. - Federal Reserve Board Governor Edward M. Gramlich warned Monday that many rural banks may soon find themselves unable to fund small-business lending.

"Small banks experience a great deal of competition for deposits from money market funds and other deposit-taking institutions," he said. "As they lose these low-cost, lendable funds, many rural banks are finding it more difficult to serve the credit needs of their customers."

This deposit drain is worsened by the transformation of rural America, he said. As farmers die, their heirs are increasingly liquidating the estate rather than continuing to work the land, he said.

"In many cases, the funds on deposit at a local bank move with the new owners and these heirs frequently live and work in metropolitan communities located far from their original homes," he said.

The rural bank comments were part of a wide-ranging speech given at a Fed-sponsored conference on small business lending. Mr. Gramlich also strongly endorsed credit scoring, saying it can eliminate many of the barriers small businesses face in obtaining credit.

"Credit scoring increases the consistency, speed, and often the accuracy of credit evaluations," Mr. Gramlich said. "It also lowers the cost of gathering relevant information."

Small businesses benefit from credit scoring because it reduces waiting time on loan approvals to "minutes or hours" from "days or weeks," he said.

Mr. Gramlich, however, warned banks to regularly check scoring models for fairness. "Bank regulators must continue to ensure that the bank's credit scoring models are accurate and nondiscriminatory," he said.

The Fed governor dismissed concerns by some that bank consolidation will hurt small business lending. Though large banks make a lower percentage of their loans to small businesses, he said credit unions, thrifts, finance companies, and insurers more than pick up the slack.

Consolidation among smaller banks actually boosts lending, he said. "When small banks buy other small banks, the new entities tend to be more active small business leaders than the banks that were purchased," he said.

At the conference, several researchers presented studies showing that banks make fewer loans in minority neighborhoods than in white communities.

Fed economist Glenn Canner found that a 10% increase in minority population in an urban area results in a 1% decline in small business lending. "Predominately minority census tracts get somewhat fewer loans," he said.

Yet Mr. Canner cautioned against overreacting to the finding, noting it is based on the Community Reinvestment Act's small business data collection requirement. The CRA data does not include information on credit demand or credit quality, and only 20% of all banks are required to file this information, he said.

Malcolm Bush, president of the Woodstock Institute of Chicago, found that banks made an average of 15 small business loans per census tract. Yet predominately black census tracts had 2.6 fewer loans per tract and Hispanic areas 5.8 fewer loans than average.

Income also affects lending, he said. Lower-income communities receive about 50% fewer small business loans than upper-income areas, while moderate-income communities get 14% fewer loans than upper income areas, he said.

"While there is not direct evidence of discrimination ... the results are generally consistent with other research showing discrimination," Mr. Bush said.

These studies were harshly criticized by Anthony Yezer, a professor at George Washington University, who said the CRA data is so flawed that it should not be used as the basis for any research. The data ignores business growth rates, competition among lenders, and credit supply, he said.

"Just because you have numbers and you yell them loudly does not mean you have anything," Mr. Yezer said.

AMERICAN BANKERS ASSOCIATION

aba.com Industry Issues

Friday, January 26, 2001

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ABA FUNDING AND LIQUIDITY STEERING GROUP

On November 13, 2000, ABA President Don Mengedoth announced the creation of a high-level "ABA Funding and Liquidity Steering Group", chaired by ABA Board Member Robert Lowe and CBC Vice-Chairman Earl McVicker. The Steering Group is made up of eleven bankers from across the nation, with the goal of examining this issue with an eye towards developing guidance and additional targeted solutions for the industry. The ABA strongly believes that such efforts are crucial to assisting community banks in their continued role as engines of local economic development in their communities.

Background

The past two decades have seen major changes in the financial services industry, with many new competitors vying for the consumer's dollar. Increased growth in mutual funds, money market funds, equity markets and the like have enticed core deposits out of banks. This shift in consumer expectations has coincided with exceptionally strong loan demand over the past decade, and the convergence of these two economic factors has caused loan to deposit ratios among banks to reach historic highs. As a result, community banks have been forced to use a variety of alternative funding mechanisms, such as Federal Home Loan Bank advances, Fed funds, loan participations, repurchase agreements, brokered CDs, loan sales, discount window, banker's banks, and asset securitization. With these efforts have come new challenges, including increased regulatory activity, shrinking interest rate margins, and asset management concerns.

Ongoing ABA Focus

Through the years, ABA has dedicated substantial resources to addressing concerns over funding and liquidity at banks and savings institutions through our work on Federal Home Loan Bank collateral issues, agricultural task-forces, the legislative creation of new savings vehicles, and the development of ABA products. Given the continued pressure faced by all banks in this area, and particularly community banks, the ABA Board of Directors has designated funding as a "super priority" issue for the ABA. The ABA's Community Bankers Council (CBC) has also, in recent meetings, cited this issue as an important concern upon which we should focus further attention. The Steering Group is an outgrowth of these concerns.

Role of Banker Steering Group

In the months ahead, the Funding and Liquidity Steering Group will explore (1) increased dialogue with the industry on current concerns and potential solutions; (2) potential legal, regulatory, and/or legislative remedies; and, (3) potential ABA products. The Steering Group will serve as a sounding board as well as a focal point, and has identified a variety of areas for further exploration. The Steering Group will explore this issue in detail, seek to define the problem(s), identify trends, increase both its profile and dialogue within the industry and with policymakers, and pursue tangible solutions which assist community banks with their funding challenges.

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ABA has established an interdepartmental staff team to support this initiative and to develop products, services and programs to help community banks in meeting the funding challenge.

January 26, 2001

Committee on Local Government
C/O Rep. Gerry Ray, Chair
State Capital, Room 115-S
Topeka, Kansas 66612

Re: House Bill No. 2086

Chair and Members of the Committee:

My schedule does not permit me to attend the hearing on the above referenced bill before your Committee, so I'd like this letter to be offered as written testimony on this proposed bill and made a part of your record:

"Valley State Bank is an independent, community bank located in Roeland Park, Johnson County, Kansas, and is locally owned by residents and taxpayers of Kansas. We do not have any public funds deposits, but are very concerned about the negative impact that this bill will have on Kansas state-chartered banks, especially those in out-state Kansas.

Municipal or public deposits are made up of Kansas taxpayer money that has been collected for the use and benefit of the Kansas taxpayer. Requiring the deposit of public funds in a bank with a "main office" in Kansas and a physical presence in the municipality serves the public interest of Kansas taxpayers and contributes to the state's economic growth and development.

Committee on Local Government-2
C/O Rep. Gerry Ray

Community banks in Kansas use deposits to fund loans in Kansas that contributes to the overall economic growth of our state. Allowing out-of-state banks to use Kansas as a "deposit gathering" operation for use in other states does not contribute to the growth and development of the Kansas economy. Loan-to-deposit ratios of Kansas's banks are at 68%, indicative of active lending to Kansas consumers and businesses.

If the $2.8 billion in public funds on deposit in Kansas banks leaves the state, there will be no multiplier effect of using these funds for loans to generate additional economic growth, development, and wealth necessary to generate taxes to provide to the benefit of Kansas taxpayers.

As a member of the Kansas State Banking Board, I'm familiar with banking conditions throughout the state. Many small community banks in out-state Kansas utilize public funds deposits to fund loans locally. They also serve an older population. If public funds flow to out-of-state banks as a result of House Bill 2086, these Kansas banks will face a severe "liquidity" or funding problem, local community loan needs will not be met, and some of these institutions will likely fail or be forced to merge.

An out-of-state bank's Community Reinvestment Act rating has nothing to do with their lending activity in Kansas. For example, World Savings and Loan Association, an Oakland, California, institution takes over $550 million in deposits out of Johnson County and over 98% of their loans are in California and four other western states.

My proposal is really simple: keep the majority of the present KSA 9-1401, but require municipalities to place public funds out for bid, disclose the bidding criteria, disclose the winning bid, and require a physical presence in the Kansas municipality and lending activity within this state. Under KSA 9-1401, if no Kansas banking institution can serve the needs of Kansas taxpayers, the municipality to go to an out-of-state institution.

Committee on Local Government-3
C/O Rep. Gerry Ray

As a Kansas resident, taxpayer, and owner of a Kansas banking corporation that pays state and local taxes, it is simply not in the public's best interests to allow Kansas taxpayers money to leave the state to fund loans in other parts of the country and negatively impact the economic growth and development of our state.

Kansas banks serve the needs of our local communities, pay taxes to the state and local governments, and use Kansas deposits to loan to consumers and businesses for homes, autos, working capital, and expansion. If Kansas banks lose the opportunity to obtain this vital funding source, consumers and businesses throughout the state will suffer.

Thank you for the opportunity to share these thoughts."

Sincerely,

Bruce B. Morgan, Ph.D.
Chairman, President & CEO
Valley State Bank

Suggested Amendments to HB 2086

9-1401. Designation of depositories for municipal and quasi-municipal funds; duty of public officers; eligible depositories. (a) The governing body of any municipal corporation or quasi-municipal corporation shall designate by official action recorded upon its minutes the banks, savings and loan associations and savings banks which shall serve as depositories of its funds and the officer and official having the custody of such funds shall not deposit such funds other than at such designated banks, savings and loan associations and savings banks. The banks, savings and loan associations and savings banks which have main or branch offices in the county or counties in which all or part of such municipal corporation or quasi-municipal corporation is located shall be designated as such official depositories if the municipal or quasi-municipal corporation can obtain satisfactory security therefor. ~~For purposes of this subsection, banks, savings and loan associations or savings banks organized under the laws of the United States or another state which do not have a main office in this state, may be designated as depositories of such municipal corporation's or quasi-municipal corporation's funds in accordance with this subsection, if such banks, savings and loan associations and savings banks have branch offices in the county or counties in which all or part of such municipal corporation or quasi-municipal corporation is located, except that such banks, savings and loan associations or savings banks shall not be eligible to receive deposits except in accordance with subsection (c).~~

(b) Every officer or person depositing public funds shall deposit all such public funds coming into such officer or person's possession in their name and official title as such officer. If the governing body of the municipal corporation or quasi-municipal corporation fails to designate an official depository or depositories, the officer thereof having custody of its funds shall deposit such funds with one or more banks, savings and loan associations or savings banks which have main or branch offices in the county or counties in which all or part of such municipal corporation or quasi-municipal corporation is located if satisfactory security can be obtained therefor and if not then elsewhere, but upon so doing shall serve notice in writing on the governing body showing the names and locations of such banks, savings and loan associations and savings banks where such funds are deposited, and upon so doing the officer having custody of such funds shall not be liable for the loss of any portion thereof except for official misconduct or for the misappropriation of such funds by such officer.

~~(c) If eligible banks, savings and loan associations or savings banks under subsections (a) or (b) cannot or will not provide an acceptable bid, which shall include services, for the depositing of public funds under this section, then banks, savings and loan associations or savings banks organized under the laws of the United States or another state which do not have a main office in this state, may receive deposits of such municipal corporation or quasi-municipal corporation, if such banks, savings and loan associations or savings banks have been designated as official depositories under subsection (a), have branch offices in the county or counties in which all or part of such municipal corporation or quasi-municipal corporation is located and the municipal corporation or quasi-municipal corporation can obtain satisfactory security therefor.~~

New subsection (c). *At such time as the deposits of such public funds mature, the officer having custody of such funds shall re-offer such funds for deposit to the eligible banks, savings and loan associations or savings banks under subsections (a) and (b).*

New subsection (d). *Upon deposit of public funds as provided in sections (a), (b) and New subsection (c), the officer having custody of such funds shall disclose to those eligible banks, savings and loan associations and savings banks participating in the bid, the winning bid including identity of the winning institution and factors used to determine the winning bid.*

9-1408. Definitions. As used in article 14 of chapter 9 of the Kansas Statutes Annotated:
(a) "Bank" means any bank incorporated under the laws of this state, or organized under the laws of the United States and which has a main office *or branch* in this state *and which maintains a Community Reinvestment Act rating of Satisfactory or above*;
(b) "savings and loan association" means any savings and loan association incorporated under the laws of this state, or organized under the laws of the United States and which has a main office *or branch* in this state *and which maintains a Community Reinvestment Act rating of Satisfactory or above*;
(c) "savings bank" means any savings bank organized under the laws of the United States and which has a main office *or branch* in this state *and which maintains a Community Reinvestment Act rating of Satisfactory or above*;
(d) "centralized securities depository" means a clearing agency registered with the securities and exchange commission which provides safekeeping and book-entry settlement services to its participants;
(e) "municipal corporation" or "quasi-municipal corporation" includes each investing governmental unit under K.S.A. 12-1675, and amendments thereto;
(f) "main office" means the place of business specified in the articles of association, certificate of authority or similar document, where the business of the institution is carried on and which is not a branch;
(g) "branch" means any office, agency or other place of business within this state, other than the main office, at which deposits are received, checks paid or money lent with approval of the appropriate regulatory authorities. Branch does not include an automated teller machine, remote service unit or similar device;
(h) "securities," "security entitlements," "financial assets," "securities account," "security agreement," "security interest," "perfection" and "control" shall have the meanings given such terms under the Kansas uniform commercial code.

12-1675. Investment of public moneys by governmental subdivisions, units and entities; conditions and limitations. (a) The governing body of any county, city, township, school district, area vocational-technical school, community college, firemen's relief association, community mental health center, community facility for the mentally retarded or any other governmental entity, unit or subdivision in the state of Kansas having authority to receive, hold and expend public moneys or funds may invest any moneys which are not immediately required for the purposes for which the moneys were collected or received, and the investment of which is not subject to or regulated by any other statute.

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12-1675, cont.

(b) Such moneys shall be invested only:
(1) In temporary notes or no-fund warrants issued by such investing governmental unit;
(2) in time deposit, open accounts, certificates of deposit or time certificates of deposit with maturities of not more than two years: (A) In banks, savings and loan associations and savings banks, which have main or branch offices located in such investing governmental unit; or (B) if no main or branch office of a bank, savings and loan association or savings bank is located in such investing governmental unit, then in banks, savings and loan associations and savings banks, which have main or branch offices in the county or counties in which all or part of such investing governmental unit is located;
(3) in repurchase agreements with: (A) Banks, savings and loan associations and savings banks, which have main or branch offices located in such investing governmental unit, for direct obligations of, or obligations that are insured as to principal and interest by, the United States government or any agency thereof; or (B) (i) if no main or branch office of a bank, savings and loan association or savings bank, is located in such investing governmental unit; or (ii) if no such bank, savings and loan association or savings bank having a main or branch office located in such investing governmental unit is willing to enter into such an agreement with the investing governmental unit at an interest rate equal to or greater than the investment rate, as defined in subsection (g) of K.S.A. 1999 Supp. 12-1675a, then such repurchase agreements may be entered into with banks, savings and loan associations or savings banks which have main or branch offices in the county or counties in which all or part of such investing governmental unit is located; or (C) if no bank, savings and loan association or savings bank, having a main or branch office in such county or counties is willing to enter into such an agreement with the investing governmental unit at an interest rate equal to or greater than the investment rate, as defined in subsection (g) of K.S.A. 1999 Supp. 12-1675a, then such repurchase agreements may be entered into with banks, savings and loan associations or savings banks;
(4) in United States treasury bills or notes with maturities as the governing body shall determine, but not exceeding two years. Such investment transactions shall only be conducted with banks, savings and loan associations and savings banks; the federal reserve bank of Kansas City, Missouri; or with primary government securities dealers which report to the market report division of the federal reserve bank of New York, or any broker-dealer engaged in the business of selling government securities which is registered in compliance with the requirements of section 15 or 15C of the securities exchange act of 1934 and registered pursuant to K.S.A. 17-1254, and amendments thereto;
(5) in the municipal investment pool fund established in K.S.A. 1999 Supp. 12-1677a, and amendments thereto;
(6) in the investments authorized and in accordance with the conditions prescribed in K.S.A. 1999 Supp. 12-1677b, and amendments thereto; or
(7) in multiple municipal client investment pools managed by the trust departments of banks which have main or branch offices located in the county or counties where such investing governmental unit is located or with trust companies incorporated under the laws of this state which have contracted to provide trust services under the provisions of K.S.A. 9-2107, and amendments thereto, with banks which have main or branch offices located in the county or counties in which such investing governmental unit is located. Public moneys invested under this paragraph shall be secured in the same manner as provided for under K.S.A. 9-1402, and amendments thereto. Pooled investments of public moneys made by trust departments under this paragraph shall be subject to the same terms, conditions and limitations as are applicable to the municipal investment pool established by K.S.A. 1999 Supp. 12-1677a, and amendments thereto.

12-1675, cont.

(c) The investments authorized in paragraphs (4), (5), (6) or (7) of subsection (b) shall be utilized only if the banks, savings and loan associations and savings banks eligible for investments authorized in paragraph (2) of subsection (b), cannot or will not make the investments authorized in paragraph (2) of subsection (b) available to the investing governmental unit at interest rates equal to or greater than the investment rate, as defined in subsection (g) of K.S.A. 1999 Supp. 12-1675a.

(d) In selecting a depository pursuant to paragraph (2) of subsection (b), if a bank, savings and loan association or savings bank eligible for an investment deposit thereunder has an office located in the investing governmental unit and such financial institution will make such deposits available to the investing governmental unit at interest rates equal to or greater than the investment rate, as defined in subsection (g) of K.S.A. 1999 Supp. 12-1675a, and such financial institution otherwise qualifies for such deposit, the investing governmental unit shall select one or more of such eligible financial institutions for deposit of funds pursuant to this section. If no such financial institution qualifies for such deposits, the investing governmental unit shall select for such deposits one or more eligible banks, savings and loan associations or savings banks which have offices in the county or counties in which all or a part of such investing governmental unit is located which will make such deposits available to the investing governmental unit at interest rates equal to or greater than the investment rate, as defined in subsection (g) of K.S.A. 1999 Supp. 12-1675a, and which otherwise qualify for such deposits.

(e) (1) All security purchases and repurchase agreements shall occur on a delivery versus payment basis.
(2) All securities, including those acquired by repurchase agreements, shall be perfected in the name of the investing governmental unit and shall be delivered to the purchaser or a third-party custodian which may be the state treasurer.

New subsection (f). *At such time as the deposits of such public funds mature, the officer having custody of such funds shall re-offer such funds for deposit to the eligible banks, savings and loan associations or savings banks under subsections (b), (c) and (d).*

New subsection (g). *Upon deposit of public funds as provided in subsections (b), (c), (d) and (e), the officer having custody of such funds shall disclose to those eligible banks, savings and loan associations and savings banks participating in the bid, the winning bid including identity of the winning institution and factors used to determine the winning bid.*

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Written Only

Kingman Kansas

City of Kingman
P.O. Box 168
Kingman, Kansas
67068-0168
Phone 316-532-3111
Fax 316-532-2147

January 26, 2001

House Local Government Committee
Kansas State Legislature
Capital Building
Topeka, KS 66612

RE: HB 2086 Banking Bill

Dear Sirs:

On behalf of the Kingman City Commissioners, I am writing to support House Bill 2086. We have had two local investment and banking firms in the last year request the opportunity to bid on city investments. They were offering a higher interest rate than we were receiving on a comparable investment. However, in both cases we had to turn down the opportunity because their institutions were not Kansas chartered.

We would like to have the opportunity to increase our local investment bid pool, which will potentially earn us a higher rate of return on our investments. This would be a great opportunity to increase revenues without increases taxes or fees.

Therefore, please support House Bill 2086.

Sincerely,

Jack Ford

Jack Ford, Mayor
Kingman City Commission

HOUSE LOCAL GOVERNMENT
1/30/01
Attachment 18

(19)

Written Only

January 26, 2001

Committee on Local Government
C/O Rep. Gerry Ray, Chair
State Capital, Room 115-S
Topeka, Kansas 66612

Re: House Bill No. 2086

Chair and Members of the Committee:

My schedule does not permit me to attend the hearing on the above referenced bill before your Committee, so I'd like this letter to be offered as written testimony on this proposed bill and made a part of your record:

"Valley State Bank is an independent, community bank located in Roeland Park, Johnson County, Kansas, and is locally owned by residents and taxpayers of Kansas. We do not have any public funds deposits, but are very concerned about the negative impact that this bill will have on Kansas state-chartered banks, especially those in out-state Kansas.

Municipal or public deposits are made up of Kansas taxpayer money that has been collected for the use and benefit of the Kansas taxpayer. Requiring the deposit of public funds in a bank with a "main office" in Kansas and a physical presence in the municipality serves the public interest of Kansas taxpayers and contributes to the state's economic growth and development.

Committee on Local Government-2
C/O Rep. Gerry Ray

Community banks in Kansas use deposits to fund loans in Kansas that contributes to the overall economic growth of our state. Allowing out-of-state banks to use Kansas as a "deposit gathering" operation for use in other states does not contribute to the growth and development of the Kansas economy. Loan-to-deposit ratios of Kansas's banks are at 68%, indicative of active lending to Kansas consumers and businesses.

If the $2.8 billion in public funds on deposit in Kansas banks leaves the state, there will be no multiplier effect of using these funds for loans to generate additional economic growth, development, and wealth necessary to generate taxes to provide to the benefit of Kansas taxpayers.

As a member of the Kansas State Banking Board, I'm familiar with banking conditions throughout the state. Many small community banks in out-state Kansas utilize public funds deposits to fund loans locally. They also serve an older population. If public funds flow to out-of-state banks as a result of House Bill 2086, these Kansas banks will face a severe "liquidity" or funding problem, local community loan needs will not be met, and some of these institutions will likely fail or be forced to merge.

An out-of-state bank's Community Reinvestment Act rating has nothing to do with their lending activity in Kansas. For example, World Savings and Loan Association, an Oakland, California, institution takes over $550 million in deposits out of Johnson County and over 98% of their loans are in California and four other western states.

<u>My proposal is really simple: keep the majority of the present KSA 9-1401, but require municipalities to place public funds out for bid, disclose the bidding criteria, disclose the winning bid, and require a physical presence in the Kansas municipality and lending activity within this state</u>. Under KSA 9-1401, if no Kansas banking institution can serve the needs of Kansas taxpayers, the municipality to go to an out-of-state institution.

Committee on Local Government-3
C/O Rep. Gerry Ray

As a Kansas resident, taxpayer, and owner of a Kansas banking corporation that pays state and local taxes, it is simply not in the public's best interests to allow Kansas taxpayers money to leave the state to fund loans in other parts of the country and negatively impact the economic growth and development of our state.

Kansas banks serve the needs of our local communities, pay taxes to the state and local governments, and use Kansas deposits to loan to consumers and businesses for homes, autos, working capital, and expansion. If Kansas banks lose the opportunity to obtain this vital funding source, consumers and businesses throughout the state will suffer.

Thank you for the opportunity to share these thoughts."

Sincerely,

Bruce B. Morgan, Ph.D.
Chairman, President & CEO
Valley State Bank