



Depository Contracts

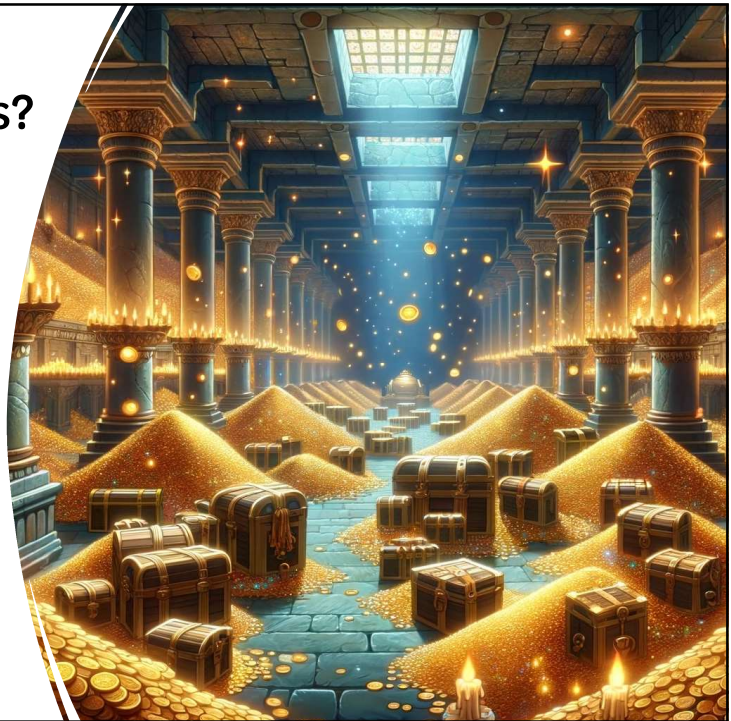
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Texas Municipal League
Public Funds Investment Act Training
March 14, 2024

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Depository Contracts? For an *hour*?

- Well, sort of... This is a Public Funds Investment Act Course, so...
- We're really talking about *Public Funds*.



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Sources of Public Funds – City Example

- Property Taxes – 35%
- Sales Taxes – 27%
- Franchise Fees – 10 %
- Permits/Fees – 7%
- Transfers from other funds – 5%
- Court Fines – 4%
- Interest Earnings – 1%
- Other Sources – 11%

What is one thing these sources have in common? Or, what is the *actual* source of public funds?




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What do We use these funds for?

- Government Services:
 - Water supply and management
 - Sewer and waste management
 - Road construction and maintenance
 - Police Protection
 - Fire protection and EMS
 - Parks
 - Land use and community development
 - Economic Development
 - Animal Control
 - And on. And on. And on...

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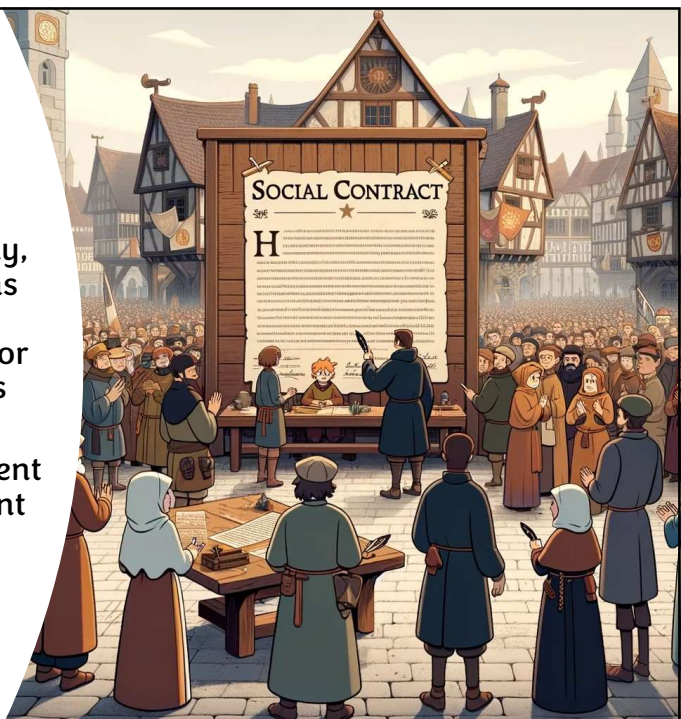
And why do I say We?

We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this Constitution for the United States of America.

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The Social Contract

- Our first contract!!
- The concept that individuals have consented, either explicitly or tacitly, to surrender some of their freedoms and submit to the authority of the ruler or government, in exchange for protection of their remaining rights and maintenance of social order.
- Part of that agreement is the payment of taxes in exchange for government services. Public Funds!



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Duty to Safeguard Public Funds

- Think of the various laws regarding use and control of public funds:
 - Conflicts of Interest,
 - Budget, Tax rate setting, & Audit Requirements
 - Public Procurement Laws
 - Open Government Laws
 - Depository Rules, PFIA, & PFCA
 - Penal Codes
 - Others...
- All of these help to reinforce the trust the people have in the government in which they entrust their security and their cash.



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Good News: We're NOT Talking About All That Today!

Depository Requirements

- Texas Local Gov't Code Chapter 105

PFIA: Public Funds Investment Act

- Texas Gov't Code Chapter 2256

PFCA: Public Funds Collateral Act

- Texas Gov't Code Chapter 2257, Subchapter B



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How These Laws Protect Trust

- Depository Rules, the PFIA and the PFCA work together to reduce:
 - Exposure to Bank Failure
 - Other Credit Risk
 - Interest Rate Risk
 - Liquidity Risk
 - Investment Allocation Risk
 - Fraud and Mismanagement



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What is a “Depository”?

The city’s “Depository” is where the city keeps its money.

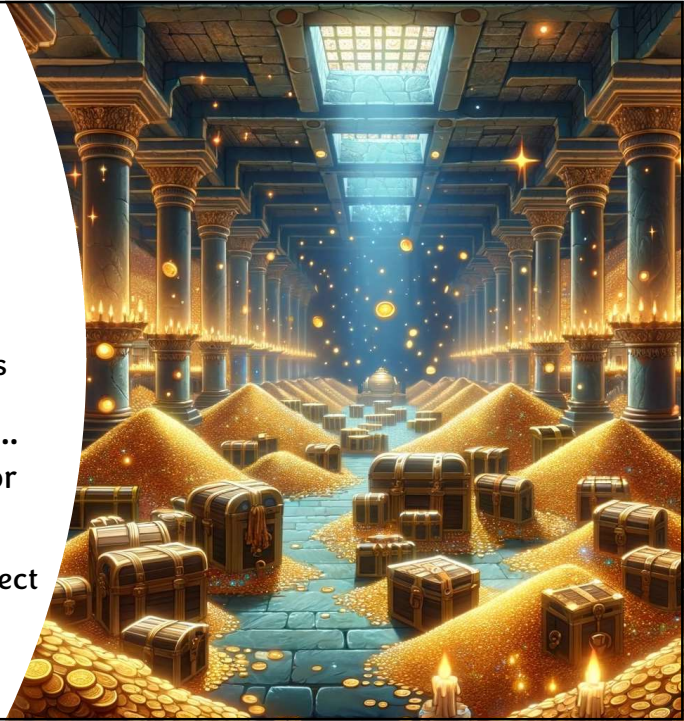
- Texas Loc. Gov’t Code Chapter 105 sets the rules
- Authorized:
 - National or State Banks or Savings Associations
 - Credit Unions
- Not Authorized:
 - Vault in a Lonely Mountain guarded by an angry dragon
 - Box full of cash in the city secretary’s office
 - Anything else!
- City can have several depositories



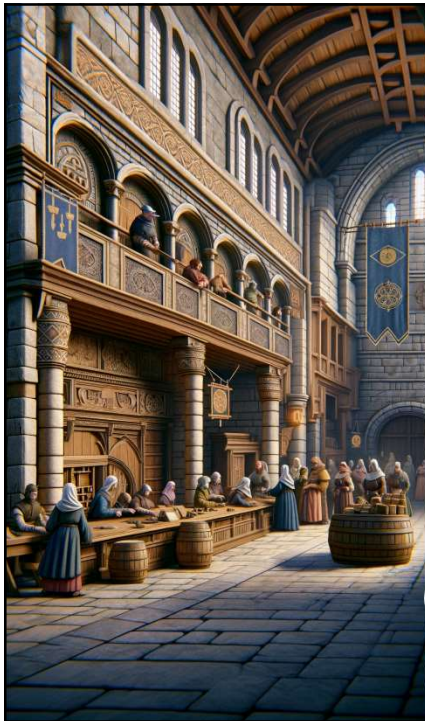
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What funds must be kept in the Depository?

- “Applies to the funds ... of any municipality or any department or agency of the municipality.”
 - General funds
 - Utility funds and other separate accounts
 - Includes interest and sinking funds
 - Forfeiture funds
 - **Nearly anything you can think of...**
- Independent entities responsible for own funds:
 - EDCs
 - Most independent entities are subject to depository law themselves



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How is a “Depository” better than my “Bank Account”?

- My Bank Account:
 - FDIC or NCUA insurance: Insures first \$250,000 of deposits, per depositor, per bank, per ownership category...
 - No additional security except that guy out front.
- Depositories:
 - Also protected by FDIC or NCUA insurance
 - Provide 100% security for deposit of public funds per PFCA.
 - Provide security for funds no later than five days before commencement of the term of the depository contract.


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What Does “Security” Mean?

- “Security” for city deposits is created when the depository provides **collateral** valued at 100% of the deposits.
- Collateral security
 - Collateral can be securities or corporate surety bonds
 - City must adopt a policy defining adequate collateral
 - Type, valuation, substitution
- Collateral is security, and securities are collateral... Round and round with the words!

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Bottom Line

If a city follows the process to select a “depository,” then **100% of the city funds** deposited in that depository are **protected against loss.**

(Remember where those “city funds” come from and how fundamentally important protecting them is.)

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What is the Process?

Just go to the closest bank and open an account in the name of the city??

- Not quite...

Public “RFA” Process

- “Request for Applications”
- City must request applications from depositories by date certain
- City must publish notice of request for applications
- Similar to RFP process, but with an “A” instead of a “P”
- Council must designate a “Designated Officer”



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Who is this “Designated Officer”?

- Treasurer or other officer so designated by city council
- Duties:
 - Gives notice of the RFA
 - Receives and reviews the applications
 - Must prepare annual report outlining details of city accounts and funds



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Notice of RFA

- Designated Officer gives notice of RFA
- The notice must contain:
 - Name and address of designated officer receiving applications
 - Date and time the applications are due
 - Date, time, and place council will consider the applications
- Notice Publication Req's:
 - 21 days or more prior to the deadline
 - In Newspaper of general circulation in the city
 - In financial publication of general circulation in the state for out-of-city options



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Which Depository Must a City Choose?

- City may reject any or all applications
- May consider all factors, including price
- **Council decision**

Limitations:

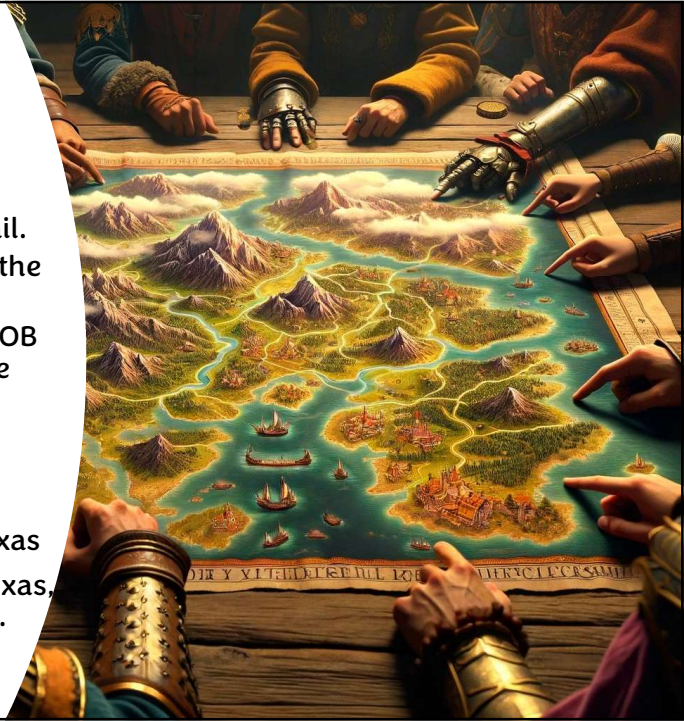
- Cannot choose an untimely submission
- Keep an eye on:
 - Depository Location
 - Council Conflicts of Interest



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Why Does Depository Location Matter?

- Because the statutes say it does...
- “**Place of Business**” is the critical detail.
 - If the depository has a POB within the city, then the city can use them.
 - If the depository does not have a POB within the city, then a city might be able to use them if:
 - The city has adopted a policy allowing for out-of-city depositories, and
 - The depository has a POB in Texas
- Credit unions must be **domiciled** in Texas, but banks can be domiciled elsewhere.



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Conflicts of Interest

- Special statute: Local Government Code § 131.903
- Does a city official or employee have an interest in the depository?
 - No? Then no problem
 - Yes? Do they have a duty to select the depository?

10% Rule

- The city **may not select** a depository in which an **official or employee** with a duty to select owns 10% or more of stock.
- Stricter than the standard city conflict rules of LGC Ch. 171
 - (Affidavit + Non-participation = Cured!)

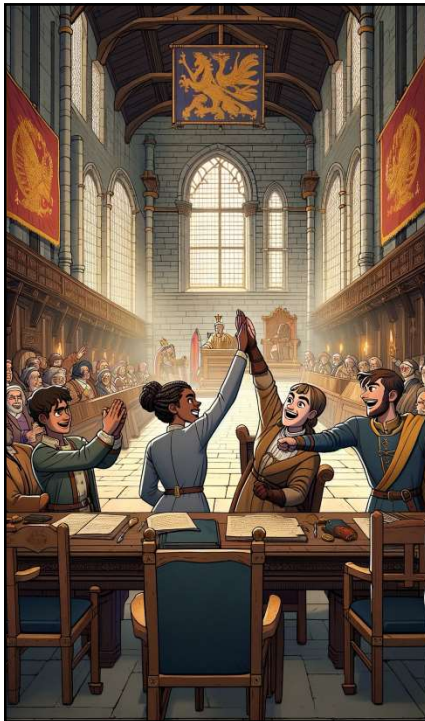
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Less than 10% Ownership...

- The city may select a depository if employee/official with duty to select owns less than 10% of stock if:
 - Conflicted individual abstains from participation and files Chapter 171 affidavit;
 - The rest of council still votes to select depository; and
 - Charter or ordinance does not prohibit the selection

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So You have Selected a Depository...

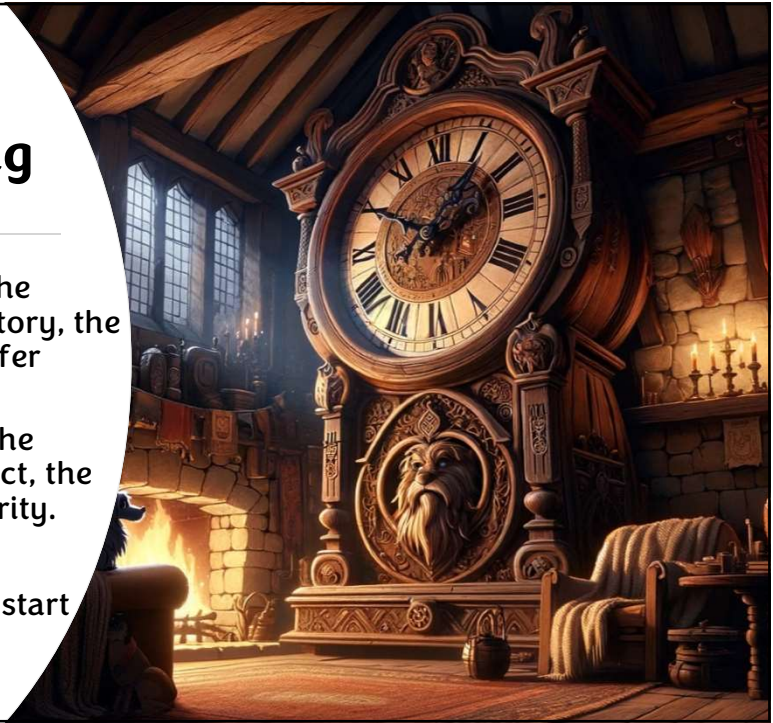
- Council must record “by order in minutes” the entity selected as depository
- **Process is not over at depository selection!!**

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The Clock is Ticking

- Not later than **60 days** after the council designates the depository, the designated officer must transfer funds.
- Not later than **5 days before** the commencement of the contract, the depository must provide security.

City can still get out of this and start process over.



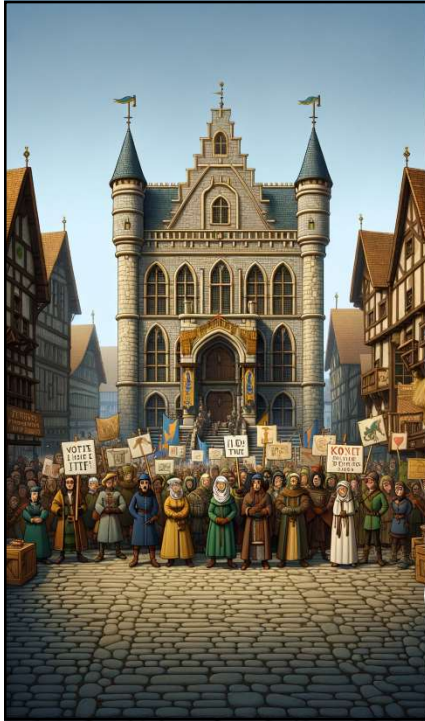
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Provisions

- Must be written
- Contract term may not exceed five years
- Provisions requiring depository to:
 - Perform all duties under the contract;
 - Keep funds covered by the contract;
 - Provide security;
 - Pay on all checks drawn;
 - Pay all transfers; and
 - Account for all city funds
- Contract may contain any provisions approved by city council
- City council **may contract for additional services** (put additional services in RFA)



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Remember Anti-Boycott Provisions

- Chapter 809, Government Code; Chapter 2274, Government Code
- **Affected Contracts and Vendors (From 2021 Legislature)**
 - Goods or **Services** contract with a value of \$100,000 or more
 - Company with more than 10 full-time employees
- **Energy Sector:** Vendor must verify in the contract that vendor:
 - Vendor must verify in the contract that vendor does not boycott energy companies and will not boycott energy companies during contract.
- **Firearms Sector:**
 - Vendor must verify that they do not have a practice, policy, guidance, or directive that discriminates against a firearm entity or firearm trade association and will not discriminate during the term of the contract.
 - Exceptions: (a) contracts with a sole-source provider, or (b) no complying bids received.

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Who Signs the Contract?

- **City:**
 - Normal practice.
 - Designated Officer?
- **Depository:**
 - Financial Institution Resource and Recovery Enforcement Act (FIRREA) requires:
 - President of bank board signs, or
 - President of loan committee signs; and
 - Contract must be entered into official depository records by resolution

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Breaching the Contract

Failure to Provide Collateral:

- Contract can be cancelled and a new depository selected if collateral is not provided
 - Zero collateral - Automatic breach
 - 80% collateral?? - Recommend cancellation.

Other breaches:

- Other breaches must be “material” to make the contract voidable
- Underline, **bold**, CAPITALIZE, increase font size if it’s important to the city!



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Is the Contract *Really* Important?

Yes, because:

- Conflict over depository breach must be brought as provided by the contract.
 - i.e., if you want to sue about it, it better be in the contract.
- Must be tried in the county where the city hall is located



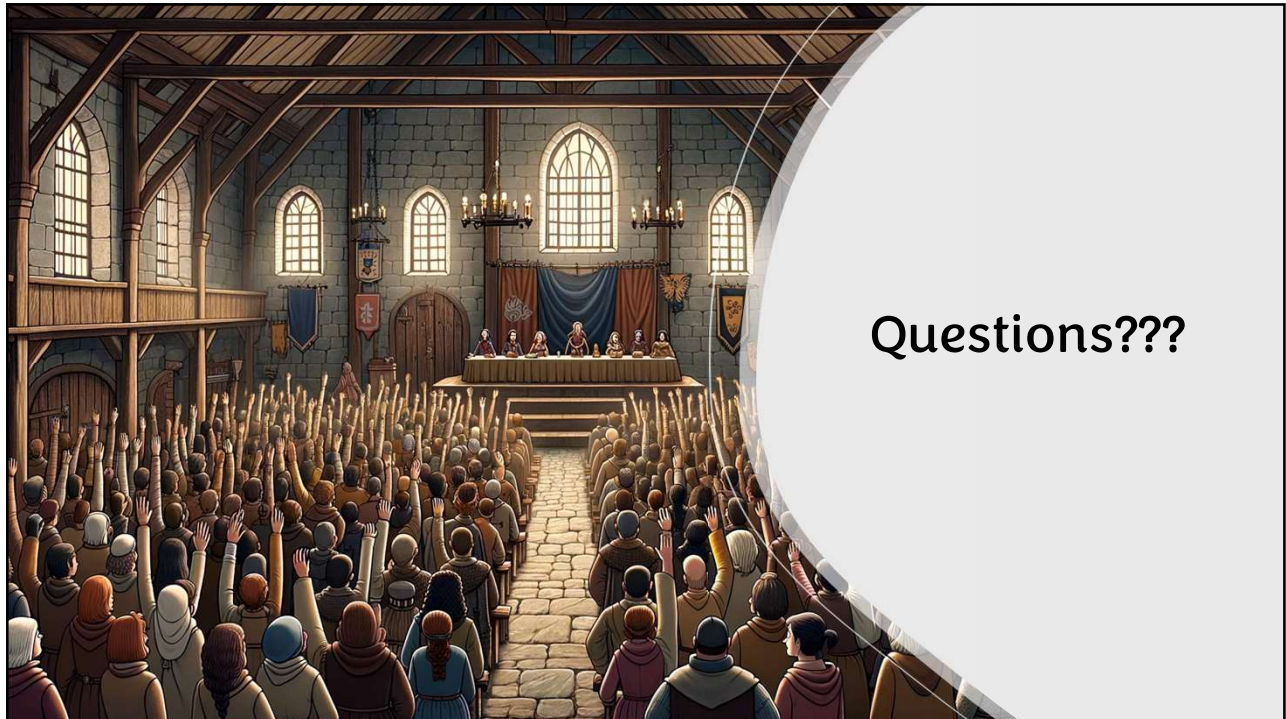
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What if the City Just Skips All This?

- **The public's funds will be at risk!!**
 - Check out the "Failed Bank List" at [FDIC.gov](https://www.fdic.gov)
 - 568 listed bank failures since 2000
- I will personally be disappointed.
- Misdemeanor for conflict-of-interest violation
- Civil suit from taxpayer
- Audit headaches



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Questions???

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