BANKING IN THE PUBLIC'S INTEREST: PROMOTING COMMUNITY DEVELOPMENT WITH THE PUBLIC DEPOSITS OF CITIES AND STATES

By

David Flax-Hatch

Edited by Kathryn Tholin

July 1991

©

Woodstock Institute, 407 S. Dearborn, Chicago, IL 60605 (312) 427-8070

THE WOODSTOCK INSTITUTE

The Woodstock Institute is a not-for-profit organization based in Chicago. For the past eighteen years, the Institute has carried out applied research and developed and implemented programs which increase private sector investment in modest-income and minority communities for the benefit of those who live there. It designs programs which bridge the gap between the needs of communities and the resources of banks, savings and loan associations, foundations and others.

The Institute provides a variety of services to community-based organizations, financial institutions, foundations and government agencies, including applied research, policy analysis, program design and evaluation.

Jean Pogge President	Kathryn Tholin Vice President

ACKNOWLEDGEMENTS

Woodstock Institute would like to acknowledge and thank the many people who gave generously of their time and ideas during the research and preparation of this report. Numerous public officials assisted in this project by participating in the written survey as well as cooperating with follow-up telephone interviews. Their information and insights were invaluable to this project.

We wish to thank the following people and organizations for their contributions:

The **National Association of State Auditors, Comptrollers, and Treasurers (NASACT)** and the **National League Of Cities** who served as partners on this project, for their input on the design of our survey, for soliciting the participation of member state and city officials, and for reviewing drafts of this report.

Thanks especially to Relmond Van Daniker, Kinney Poynter, and Albert Hrabak of NASACT and to Doug Peterson, Virginia Mayer, and Bill Barnes of the National League of Cities for their thoughtful insights and their ongoing support and assistance.

Thanks to Woodstock Institute staff, Patricia Woods and Beverly Berryhill, for their substantial contributions in the production of this report, and to Anne Gilson, for her assistance in the tabular and graphic presentations in this report.

A very special thanks to Kathryn Tholin of Woodstock Institute who edited and collaborated on this publication. Ms. Tholin asked good questions, brought greater clarity to the presentation of this research, and substantially revised this text. Her insights and contributions are greatly appreciated.

Woodstock Institute takes full responsibility for the content and recommendations in this report.

EXECUTIVE SUMMARY

State and municipal governments hold billions of dollars in tax, fee and other revenues which must be deposited or invested until the time of their appropriated expenditure. While public funds have traditionally been deposited with two criteria in mind, those of safety and return, some states and cities have begun to look at the uses to which public investment dollars are put, as a third criteria for making deposit decisions. This third criteria allows state and municipal governments to leverage new and different kinds of private investment to meet the economic and development needs and goals that they have defined.

Development-oriented deposit programs offer great potential for stretching public resources to leverage increased private investment. They have the advantage of using public funds to support public goals without actually spending them. Although some programs incur the cost of foregone interest earnings, it is a cost potentially far outweighed by the benefits created in terms of new housing, jobs, increased tax revenues, and reduced public expenditures that would have been spent for direct programs.

This study details Woodstock Institute's research into existing public deposit programs. Through a national survey, development-oriented deposit programs were identified and detailed information on these programs was gathered through surveys and interviews.

Development-oriented uses of public deposits are not yet common, but are expanding in number and scale. At least seventeen states and sixteen cities have implemented some type of development-oriented deposit program. While one program has been in effect for 22 years, several of the programs are quite new, having been implemented within the past two years. Despite enormous diversity in design and scale, these programs have many common elements and face common problems.

There are two basic types of development-oriented deposit initiatives: incentive deposit programs and linked deposit programs. **Incentive deposit programs** either "screen" potential depositories based on reinvestment performance to eliminate those with substandard performance from selection as public depositories or "reward" depositories with deposits and depository business for exemplary performance in specified areas of lending. **Linked deposit programs** make a specific deposit, often at a below-market rate of interest, to enable a specific loan or lending program with similar interest rate discounts to occur. In either case, the deposit of public funds is used to leverage private resources to address community needs.

Incentive deposit programs seek to have a broad impact on overall policies and lending patterns of financial institutions through utilizing the leverage of public deposits. To evaluate the reinvestment performance of financial institutions, incentive programs rely upon the collection and analysis of data disclosed by institutions applying for deposits. The type of disclosure required depends on the city or state's defined credit needs and areas of concern, but may include aggregate or geographic reporting of various types of lending, participation in government sponsored development efforts, branch openings and closings, affirmative action hiring and affordable financial services for low- and moderate-income residents.

Incentive programs have historically struggled with clearly defining data disclosure reporting requirements, establishing a quantifiable and yet flexible system for evaluating general reinvestment performance as well as performance in specific areas, and implementing procedures that ensure that reinvestment considerations are institutionalized within the depository selection and deposit making processes. In many cases these details have been left to finance officers without sufficient resources or input from development practitioners. Despite these challenges, administrators of the most active incentive programs report that new reinvestment initiatives by financial institutions have resulted from their program.

Linked deposits target specific areas of needed investment and use public deposits to leverage targeted lending. Despite the small number of existing programs, Woodstock Institute's research reveals that over $1 billion is currently invested in linked deposits. Some programs devote substantial portions of their deposit funds to linked deposit programs. Missouri and Ohio invest 35% and 12% of their total funds respectively in linked deposits. Overall, however, linked deposits represent only one percent of total deposits reported by 64 cities and 30 states. Linked deposits have been used to support state farm economies through planting season loans, to encourage small business lending, to attract major employees and to enable rehabilitation of affordable housing.

Linked deposit programs face their own set of challenges. They must identify credit needs of importance to the city or state which are not adequately met or require special assistance such as is offered in below-market rate lending. Monitoring is needed to ensure that banks are making linkage loans in accordance with agreed upon conditions and to ensure that loans are being used for the purposes designated. To be most effective, the impact of linked deposit programs need to be periodically assessed to determine whether they are bringing about desired results and truly serving as an needed incentive.

While most administrators of linked deposit programs believe that their programs are having the desired impact and leveraging net new funds and/or lending that is otherwise difficult to obtain, only one impact study has been undertaken to date. Finally, collateral requirements often serve as a disincentive for financial institutions to participate in a linked deposit program, because they require financial institutions both to make targeted loans and to hold collateral in exchange for the deposits.

While development-oriented deposit programs are growing and new programs are being implemented, their scale and impact remains far short of their potential. Analysis of each type of program, incentive deposits and linked deposits, points to lessons learned which can strengthen and expand development deposit programs.

Incentive programs are most easily implemented when standards for evaluating the performance of financial institutions are objective and easily measured. In the future, the new CRA rating systems and evaluations may provide a tool for simplifying data collection and analysis. Incentive programs have also been most effective when they are designed to leverage new commitments and involvement by financial institutions, involve agencies and staff with development needs and expertise, and are flexible enough to respond to special efforts by financial institutions.

Linked deposit programs could be more easily expanded through the development of ways to ease high collateralization requirements. The use of pension funds, which often carry larger levels of deposit insurance, and the development of collateral pools to provide additional insurance are among the measures which should be explored. The impact of linked deposit programs is also maximized through their coordination with other public and private development programs.

In addition, both types of programs could benefit from greater visibility and marketing within their areas. Officials in cities and states without development-oriented deposit programs need sources of information on program design and implementation. Finally, further evaluation of the local economic impacts of these programs would provide information which would aid cities and states to design new programs or modify existing programs.

TABLE OF CONTENTS

	PAGE
I. INTRODUCTION	1
II. DESCRIPTION OF STUDY	3
III. LINKED DEPOSIT PROGRAMS	5
Existing Linked Deposit Programs	6
Size of Existing Programs	7
Types of Eligible Lending of Linked Deposit Program	8
Key Features of Linked Deposit Programs	14
Summary	22
IV. INCENTIVE PROGRAMS	25
Existing Reinvestment Incentive Programs	28
Disclosure Provisions and Data Analysis	31
Analysis of Disclosure Data	33
Depository Selection and Decision Making	36
Program Evaluation	38
Summary	38
V. FEATURES OF PUBLIC DEPOSIT PRACTICE	41
Making Depository Selections	41
Interest Rate Requirements on Public Deposits	42
Collateralization Requirements	44
Eligible Depository Institutions	48
Distribution of Public Deposits	51
VI. CONCLUSIONS AND RECOMMENDATIONS	61
Incentive Programs	62
Linked Deposit Programs	64
Recommendations	66
General Recommendations	70
APPENDIX I	
Linked Deposit Program Profiles	

CHARTS

		PAGE
CHART 1	LINKED DEPOSIT AMOUNTS BY STATE	7
CHART 2	LINKED DEPOSIT AMOUNTS BY CITY	8
CHART 3	STATE LINKED DEPOSIT PROGRAMS ELIGIBLE LOAN TYPES	9
CHART 4	MUNICIPAL LINKED DEPOSIT PROGRAMS ELIGIBLE LOAN TYPES	14
CHART 5	FEATURES OF STATE LINKED DEPOSIT PROGRAMS	18
CHART 6	INCENTIVE DEPOSIT PROGRAM	27
CHART 7	DETERMINATION OF MINIMUM ACCEPTABLE INTEREST RATE--STATES	43
CHART 8	DETERMINATION OF MINIMUM ACCEPTABLE INTEREST RATE--CITIES	43
CHART 9	PERCENTAGE OF COLLATERAL REQUIRED ON PUBLIC DEPOSITS--STATES	45
CHART 10	PERCENTAGE OF COLLATERAL REQUIRED ON PUBLIC DEPOSITS--CITIES	46
CHART 11	ELIGIBLE DEPOSITORIES BY TYPE--CITIES	49
CHART 12	ELIGIBLE DEPOSITORIES BY TYPE--STATES	50
CHART 13	DISTRIBUTIONS OF DEPOSITS BY INSTITUTION TYPE--STATES	52
CHART 14	DISTRIBUTIONS OF DEPOSITORIES BY INSTITUTION TYPE--CITIES	53
CHART 15	DISTRIBUTION OF STATE FUNDS	54
CHART 16	DISTRIBUTION OF MUNICIPAL FUNDS	57

I. INTRODUCTION

Each year, state and local governments collect billions of dollars in taxes along with license, service, and other fees. These funds are deposited or invested until they are needed to pay for appropriated expenditures. Traditionally, these funds have been deposited or invested based upon two criteria: safety and rate of return.

Yet, limiting investment criteria to these two factors neglects the power of public funds to leverage investments which address public goals. When public deposit decision-making includes the uses to which the public's investment dollars are put, in addition to safety and return, the public's funds can be used in ways which address local credit needs and bring maximum benefit to the local economy.

During the past two decades, there have been a number of such public deposit efforts and initiatives in cities and states across the country. These efforts have been designed to influence the lending programs of local institutions by awarding deposits to institutions with good reinvestment records, or by enabling specific targeted lending programs.

These public deposit initiatives have included two types of approaches. Incentive deposits connect a financial institution's access to public deposits with its reinvestment or development lending performance. Depositories may be screened to meet minimum reinvestment criteria, or institutions may be "rewarded" with public deposits based on their reinvestment performance. Linked deposits are funds which are deposited, often at reduced interest rates, to leverage a specific lending program. Linked deposit programs target lending to particular areas of local need, such as job creation or affordable housing, in order to enable loans which might not otherwise be possible.

Policy initiatives that use public deposits to promote community development goals or programs have been scattered and poorly publicized. Yet, for several reasons, such initiatives hold promise for state, municipal, and other government entities seeking to address pressing economic problems and needs with limited and sometimes shrinking resources. These include:

1) Reinvestment-oriented deposit programs use public local resources to promote local public goals without actually spending those funds. The net benefits of linked deposits to the city or state including housing or jobs created additional tax revenues generated as a result of new or

increased economic activity and other economic benefits of specific projects, are likely to be significant when compared to the opportunity costs from reduced interest rates on deposits. In addition, because the city or state is not directly supporting these projects or creating new public programs to do so, actual public outlays are reduced.

2) Reinvestment deposit programs provide an incentive to increased community reinvestment activities by private financial institutions and promote their active participation in the process of economic development and development finance.

3) Public funds represent an enormous resource, the total of all government revenue. Even a small portion of this money, directed to economic goals through leveraging private finance, translates into billions of dollars of additional targeted investment.

4) Such initiatives can be an effective complement to the federal Community Reinvestment Act requirements for lending institutions and can provide an additional incentive for effective private reinvestment programs.

This publication presents the results of Woodstock Institute's research into the current use of public deposits to promote economic development and community research. This research draws upon several sources of information including a national survey of public deposit practices of states and cities, discussions with various government officials involved in legislative or programmatic attempts to use public deposits to promote development, the review of documentation on a number of existing programs, practical experience of the Institute in designing specific linked deposit programs, and interviews with representatives of the banking industry.

This publication also includes our findings and recommendations regarding the state of the art of public deposit practice and the opportunities, obstacles, and questions involved in using public deposits to promote the private financing of public economic development priorities.

Today, when public funds are an especially scarce resource, it is imperative that the greatest impact possible is achieved with limited dollars. This publication is designed as a resource for public financial officials, city and state development officials, community organizations, and leaders who are seeking to implement public deposit initiatives or to improve existing programs. A companion publication, "(to be published)", will serve as a "how-to" guide for those seeking to implement a public deposit initiative.

II. DESCRIPTION OF STUDY

The purpose of this study is to explore the existence of, and the potential for, state and local government efforts to use public deposits to promote community development and reinvestment. In order to achieve this purpose, Woodstock Institute sought to identify existing development-oriented uses of public deposits and to draw from these programs elements and components of success as well as problems, limitations, or impediments. Ultimately, this research is meant to assist in wider and more effective use of public deposits to promote community development and reinvestment.

This publication presents the results of several types of research. The core of data and information used in this publication is derived from a national survey of state and municipal governments to gather information on public deposit policies. This survey was completed in partnership with the National League of Cities and the National Association of State Auditors, Comptrollers and Treasurers (NASACT), who assisted in development and distribution of the survey and review of results.

The survey targeted all 50 states and all cities with populations of 100,000 or more (283 cities in all). Thirty-six states and 101 cities responded to the survey. The survey solicited information on incentive and linked deposit programs as well as on general public deposit policies and practices that inform or affect the potential and nature of such initiatives. States and cities indicating that they had some form of development- or reinvestment-oriented program were asked to provide additional information and documentation on their programs. Follow-up phone interviews were made to supplement information on these programs as well as to clarify any other survey responses that were ambiguous. Of those cities and states with development-oriented programs, phone interviews were conducted with a knowledgeable staff person in 12 of 17 states and ten of 16 cities.

This publication also draws upon interviews with several representatives of the banking industry. These interviews were designed to inform this research with an industry perspective on both the potential and the impediments of the various types of programmatic approaches.

This research also draws upon the Institute's substantial practical experience in the area of incentive and linked deposits. Woodstock Institute has designed and provided technical assistance on several linked deposits under the

Illinois Specific Opportunities Program; has conducted research on the Chicago Municipal Depository Ordinance; and has provided technical assistance to various city officials across the country.

Finally, this research draws upon the Institute's 18 years of experience in research, program design, technical assistance, and policy development work in the area of community reinvestment.

It should be noted that in several cities and states, the understanding of the nature and practical conduct of incentive or linked deposit programs differed between interested and knowledgeable parties. This publication attempts to provide accurate information on the basic design and operation of these programs without taking sides or making evaluations about their success, except to the extent that such evaluations tended to be commonly corroborated among interested parties. One of the key findings of this report is that states and cities with public deposit programmatic initiatives have not undertaken any systematic study of their impact or success. Woodstock Institute did not attempt to undertake such evaluations because they were not possible within the scope of this study.

III. LINKED DEPOSIT PROGRAMS

Linked deposits are funds which are specifically linked to an individual loan or a targeted lending program. Linked deposits usually earn an interest rate that is below the usual market rate for the type of deposit made and are used to "leverage" loans that also carry interest rates that are below market rates. By reducing the cost of funds to the financial institution, the government's deposit enables the financial institution to reduce the cost of loans to borrowers. Linked deposit programs usually target particular areas of need in the city or state, such as affordable housing or job creation, and use public deposits to directly leverage private lending in these areas.

There are two key factors that are essential to understanding linked deposit programs:

First, linked deposit programs target specific areas of economic activity that the public entity wishes to promote. Targeted areas may be as general as job creation and home ownership or as specific as support to enable small minority-owned businesses to bid on public contracts. The lending targeted by linked deposits is defined by public policy goals.

Second, linked deposit programs seek to promote loans that are difficult to obtain or might not be possible without reduced loan costs. There may be a number of reasons for this, including:

1) The targeted lending includes areas of economic activity that are traditionally underserved, or ignored by the private market, because of the perception that the loans are more risky and/or unprofitable. Such areas often differ between cities and states but may include lending in low-income neighborhoods or lending for small businesses, affordable housing, or small scale agricultural production.

2) Public deposits are needed by a smaller institution that is willing and well placed to do lending but does not have a deposit base to support the scale of lending activity needed.

3) The success of a particular project is contingent upon a cost subsidy which can be provided through a reduced rate of interest on the public deposit.

4) The short-term nature of most large deposits has made it more difficult for financial institutions to offer long-term and/or fixed rate loans.

By solving one or more of these problems, governments promote economic activity that would be unlikely to occur otherwise.

The design of linked deposit programs entails consideration of a number of specific factors. Among these are: 1) the program's goals and objectives, specifically the types of loans and lending it will seek to leverage; 2) the process for applying and qualifying for a linked deposit; 3) criteria for determining eligibility and compliance, such as business size restrictions, job creation commitments and income or geographic characteristics of borrowers; 4) the term of the deposit and often of the loan it leverages; 5) the interest rate of the deposit and any guidelines for matching deposit rates to loan rates; 6) disclosure or reporting requirements for participating financial institutions and review or evaluation procedures for the sponsoring public entity; and 7) statutory and regulatory requirements applying to public deposits which may affect linking deposits, including interest rate restrictions, collateralization requirements, and bid procedures.

Existing Linked Deposit Programs

Woodstock Institute's written survey of cities and state identified seven municipalities (of 101 responding) and 15 states (of 36 responding) which had authorized or implemented linked deposit programs.

The seven cities are: Akron, Ohio; Concord, California; Kansas City, Kansas; Kansas City, Missouri; Lansing, Michigan; Raleigh, North Carolina; and Torrance, California.

In addition, Minneapolis indicated that while it did not have an established linked deposit program it has occasionally issued individual linked deposits in the past.

The 15 states are: Illinois, Indiana, Iowa, Kansas, Louisiana, Maine, Maryland, Michigan, Missouri, Montana, Ohio, Pennsylvania, Texas, West Virginia, and Wyoming.

Three of these states reported that their linked deposit programs are no longer active. Kansas had a linked deposit program utilizing special funds which became unavailable in 1989. Efforts to establish a new program through legislation failed, primarily due to a lack of monitoring capacity in the Treasurer's Office.

Michigan has lent out all funds authorized for linked deposits and reported no current activity.

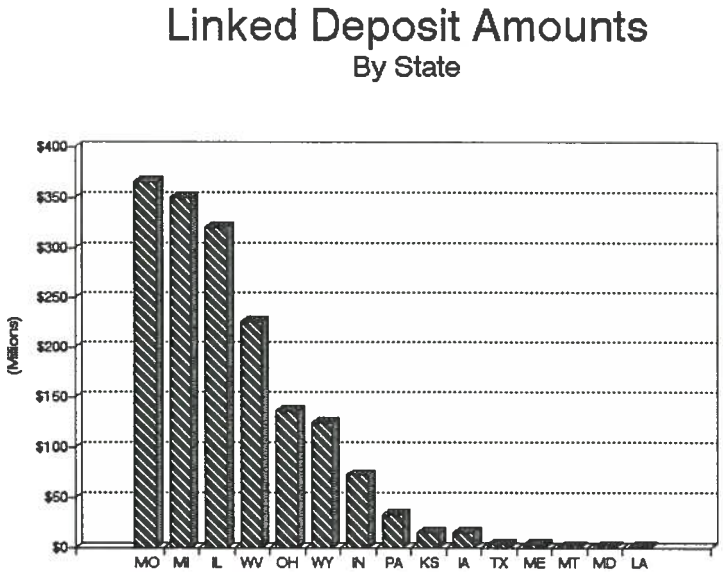
West Virginia administered a linked deposit program from 1986-1989, but the program was suspended in 1989.

Although two of the 15 states recently suspended funding for its program and a couple of others have had little or no recent activity, at least 11 state programs are currently active.

Size of Existing Programs

The combined value of funds deposited under the state linked deposit programs (reported for 1989 or most current annual cycle) was more than one billion dollars ($1,002,240,000). Three of the 15 states reported no funding of linked deposits in the most recent year. Annual funding levels ranged from a low of $150,000 by Louisiana to a high of $365 million by Missouri (see Chart 1). Of those which had made linked deposits in the most recent year, total linked deposits ranged from 0.1% of total public deposits (Montana) to 35% (Missouri). Illinois ranked second to Missouri in percentage of public deposits in linked deposits, with 8%. Only seven states allocated more than one percent of their total deposits to linked deposits.

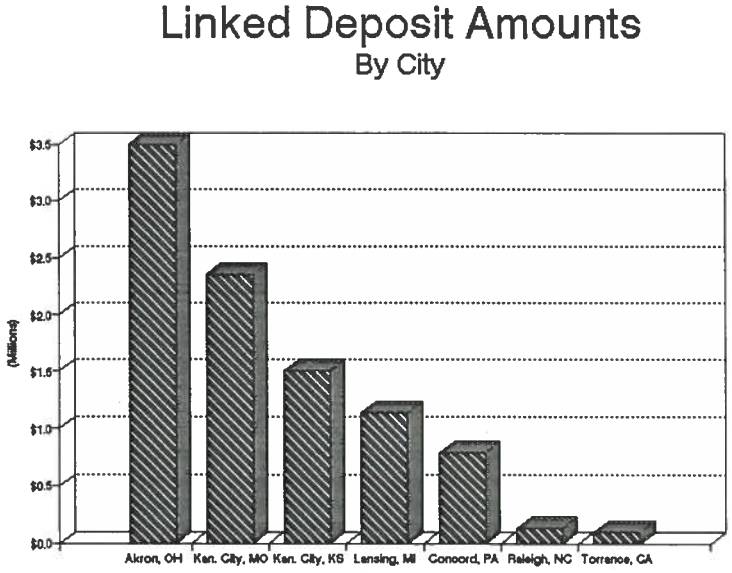
CHART 1



Ten states reported that specific allocations were made to their linked deposit programs. Among these ten, actual deposits constituted 74% of total allocations. Individually, the percentage of allocated funds actually deposited under the various linked deposit programs ranged from a low of 0.4% for Louisiana to 100% by Indiana and Kansas.

Municipal programs are of a much smaller scale than state programs. This correlates with the overall fiscal profile of cities, which have fewer dollars overall and a smaller proportion of long-term deposits. The combined reported value of funds deposited under the seven cities that reported information on their linked deposit programs was $8 million. Sums actually deposited under the municipal programs ranged from a low of $92,000 (Torrance, California) to a high of $3.5 million (Akron, Ohio). Two of the seven municipal programs deposited less than $500,000 in linked deposits in the most recent year. Only three cities deposited more than $1 million under their linked deposit program in the most recent year (see Chart 2).

CHART 2



Among the six cities that allocated specific sums to their linked deposit programs, three cities deposited 100% of their allocation, two cities deposited more than they allocated, and one city deposited 47% of its allocated funds. One city, Raleigh, N.C., made $125,000 in linked deposits without making any specific allocation.

Types of Eligible Lending of Linked Deposit Programs

Cities or states may consider a wide range of loan purposes eligible for linked deposit programs: loans for the purchase, rehabilitation, and construction of housing; loans to non-profit developers; loans to small, minority, or women-owned enterprises; and agricultural loans. Each program is designed to reward the types of loans determined to be priorities in a

particular state or city. Linked deposit programs may promote a wide range of development goals or target very specific areas of development or even individual development projects.

State Programs

Agriculture and small business are the two types of economic activity most commonly targeted by the state linked deposit programs (see Chart 3). Twelve of the 14 states that reported their lending targets identified agriculture and eleven identified business as areas of lending focus. In three states, Indiana, Texas, and Michigan, linked deposits were focused solely on lending for agricultural purposes. In addition to agriculture, every other state included business lending in their linked deposit goals.

CHART 3

STATE LINKED DEPOSIT PROGRAMS
Eligible Loan Types

	AGRICULTURE	COMMERCIAL General	COMMERCIAL Small Business	HOUSING	OTHER
MARYLAND	–	–	Ys	–	–
KANSAS	Ys	–	Ys	–	–
INDIANA	Ys	–	–	–	–
WEST VIRGINIA	–	–	–	–	–
MICHIGAN	Ys	–	–	–	–
TEXAS	Ys	–	–	–	–
WYOMING	Ys	Ys	–	–	–
IOWA	Ys	–	Ys	–	Ys
ILLINOIS	Ys	Ys	Ys	Ys	–
PENNSYLVANIA	–	–	Ys	–	–
MONTANA	–	Ys	–	Ys	–
OHIO	Ys	–	Ys	–	–
LOUISIANA	Ys	–	Ys	–	–
MAINE	Ys	Ys	–	–	–
MISSOURI	Ys	–	Ys	–	Ys

The popularity of agricultural linked deposit programs stems from the central role that credit availability plays in the farm crisis of the past decade. This type of linked deposit also is a natural outgrowth of other types of governmental support for farming, especially small farms. Another reason for their popularity is the fact that agricultural loans funded by linked deposits tend to be short-term loans tied to crop cycles, and therefore lend themselves to the annual budgeting cycles and short-term deposit practices of state government.

Small business promotion has been a major focus of public and community economic development and job creation efforts during the past decade. A very large body of research has emphasized the role of small business in creating the majority of new employment opportunities and

LINKING DEPOSITS TO AFFORDABLE HOUSING

Program:	Missouri's MO BUCKS Linked Deposit Program
Purpose:	Affordable Housing Rehabilitation Loan
Amount:	$240,000
Instrument:	Renewable 12-Month Certificate of Deposit
Deposit Rate:	300 basis points below U.S Treasury Bill rate
Loan Rate:	300 basis points below bank's lending rate
Participants:	State Treasurer Boatmen's Bank of St. Louis O'Fallon 2000 (not-for-profit developer) Missouri State Development Agency.
Result:	Rehabilitation of ten units of Section 8 affordable housing in previously vacant buildings.

In June of 1990, Missouri expanded its MO BUCKS linked deposits program into housing with a linked deposit to support the rehabilitation of ten units of abandoned housing for occupancy by low-income families. Having secured 55% of its financing from the Missouri Community Development Agency, O'Fallon 2000, a nonprofit developer sought private financing for the rest. In cooperation with the state's Development Agency, the State Treasurer leveraged the private financing of the remaining 45% through a reduced rate linked deposit with Boatmen's Bank of St. Louis. This deal resulted in the rehabilitation of four vacant buildings totaling ten units of housing for occupancy by low-income residents in north St. Louis.

LINKING DEPOSITS TO HUMAN SERVICES

Program: Iowa Linked Investments For Tomorrow

Purpose: Child Care Center

Amount: $20,000

Instrument: Renewable 12-month Certificate of Deposit

Deposit Rate: 5.27%

Loan Rate: 9.27%

Participants: Wee Care Child Care Center
Iowa State Treasurer
Farmers State Bank
Iowa Department of Economic Development

Result: Establishment of child care center and the creation of eight jobs.

In 1989, the Iowa State Treasurer linked a deposit to a loan for the establishment of a child care center for Nashua, Iowa. Upon the referral from the Iowa Department of Economic Development, the Wee Care Center applied for a linked deposit through the Farmers State Bank of Plainfield, Iowa. The linked deposit CD carried a 5.27% rate, allowing the bank to realize a 4% spread and still make a loan at a below-market rate of 9.27%. The loan was used to secure property and equipment for the start up of the child care center. In addition to providing needed child care services, this linked deposit resulted in the creation of eight jobs.

LINKING DEPOSITS TO STRENGTHENING COMMUNITY INTERMEDIARIES

Program: Illinois Linked Deposits Program

Purpose: Capitalization of a Community Loan Fund

Amount: $5 million

Instrument: 3-year fixed rate CD

Deposit Rate: 6.2%

Participants: State Treasurer
South Shore Bank
Chicago Community Loan Fund

In January 1991, the State of Illinois announced a $5 million linked deposit designed to help capitalize the Chicago Community Loan Fund. This linked deposit, designed to achieve a two-pronged impact, is unique in several ways.

Rather than provide linkage to a specific loan, this linked deposit seeks to assist in the establishment and capitalization of a new lending intermediary. The Chicago Community Loan Fund seeks low-interest loans from private individual and institutional investors, relending those funds to local community development projects. Funds raised through the linked deposit will contribute to startup of the Fund's operations and the establishment of a loan-loss reserve. The reserve fund will enhance the Fund's ability to attract loan funds from its targeted market of individual and institutional investors.

To provide this support to the Loan Fund, the State Treasurer structured a two-part interest payment. The State's deposit was made at a fixed rate of 6.2%, 105 basis points below market rate at the time of deposit. The 105 basis points spread is paid to the Chicago Community Loan Fund.

In addition to support of the Loan Fund, the State's deposit will enable additional community development lending. The State Treasurer's deposit was made to South Shore Bank, the nation's foremost development bank, located in a mixed-income black community on Chicago's south side. By placing the linked deposit in South Shore Bank, the State of Illinois was able to ensure that its deposit dollars would be reinvested in badly needed loans by a financially sound bank with an exceptional track record in community development lending.

This two-pronged lending impact was ensured because the state's deposit was made from funds which did not require the bank to pledge collateral. This means that the deposit is available to the bank as a source of loan funds.

small business development has become a focal point of economic development efforts, especially in northeastern industrial states that have lost manufacturing jobs during the past ten to 15 years. A second influence on economic development activity has been the widely-held belief that women and minorities have less access to capital and credit and need more assistance in securing business credit. Among the 12 states with small business components to their linked deposit programs, six specifically targeted minority- and women-owned business development as part of their small business focus. Business lending fits well into a linked deposit framework because the terms on these loans tend to be shorter and more equally match the term of deposits offered by most state linked deposit programs.

Housing-related linked deposits generally seek to increase the affordability of housing and home ownership by reducing the cost of financing through interest rate reductions. One potential difficulty to linking public deposits to housing loans is that they are much longer-term loans than business loans and are difficult to match with deposits for the duration of the loan. Only two states, Illinois and Montana, have linked housing loans to their public deposits. Both of these states have made housing construction, housing rehabilitation, and mortgage loans eligible for linked deposits. Housing initiatives are more common in city public deposit programs. The lack of state linked deposit programs for housing lending is particularly curious given the significant decline of federal funds for housing programs during this period.

Three states, Illinois, Montana, and Missouri, allowed deposits to be linked to loans to nonprofit organizations. Although loans to nonprofits were not necessarily limited to nonprofit community developers, such organizations have had a growing impact on community-based development efforts and frequently rely upon subsidies including below-market linked deposit loans for their projects.

A handful of other types of loans were eligible for linked deposits in four of the states. The more general categories of job retention and community development lending were each identified as eligible for linked deposits in one state. One state made student loans eligible for linked deposits. Two states indicated that commercial loans to large corporations were eligible for linked deposits, at least in some circumstances. One state specified that alternative agriculture, horticultural and exotic animal ventures were specifically targeted under their program, in addition to loans for building facade rehab projects.

Municipal Programs

Unlike state linked deposit programs which focussed primarily on commercial or agricultural loans for job creation, municipal linked deposit programs concentrate more heavily on residential lending programs (see Chart 4). Six of the seven cities linked their deposits to some form of housing lending (all but Kansas City, Kansas). All six of these cities linked deposits to home improvement or rehabilitation loans. In addition to rehabilitation loans, Raleigh linked deposits to mortgages for low- and moderate-income buyers while Concord, and Kansas City, Missouri linked deposits to mortgages and home construction loans. Of these six cities, only Kansas City, Missouri, did not restrict its linked deposits to housing lending, being the only city to link its deposits to commercial loans for small businesses. Kansas City, Kansas, conducted a special linked deposit program to renovate an office building in order to attract a major employer.

CHART 4

MUNICIPAL LINKED DEPOSIT PROGRAMS
Eligible Loan Types

	HOUSING			COMMERCIAL	OTHER
	Mortgages	Rehab	Construction		
Akron, OH	---	Yes	---	---	---
Concord, MA	Yes	Yes	Yes	---	---
Kan. City, KS	---	---	---	---	Yes
Kan. City, MO	Yes	Yes	Yes	Yes	---
Lansing, MI	---	Yes	---	---	---
Raleigh, NC	Yes	Yes	---	---	---
Torrance, CA	---	Yes	---	---	---

Key Features of Linked Deposit Programs

Interest Rates

Reduced interest rates are a key feature of linked deposit programs. Reduced rates are an attractive incentive to participation by depository institutions and are an effective way of reducing project costs for borrowers.

Every one of the states and cities with active linked deposit programs provides for reduced interest rates on their deposits to leverage loans. Most states tie the interest rate of their linked deposits to particular deposit or investment instruments, such as bank certificates of deposit (CDs) or U.S. Treasury bills (T-Bills). Four

LINKING DEPOSITS TO JOB CREATION

Program: Kansas City, Kansas

Purpose: Attract major employer to create jobs

Amount: $1.5 million (initial deposit)

Instrument: 10-year declining balance deposit

Deposit Rate: 0%

Loan Rate: 4%

Participants: City of Kansas City
Wyandotte County
Board of Public Utilities
Gateway Centre Inc. (a developer)

Result: Relocation of a HUD office with 260-300 jobs.

Although the city of Kansas City, Kansas, does not have an ongoing linked deposit program, the city designed a creative intergovernmental linked deposit that resulted in the addition of over 250 jobs to the city. In order to make the relocation of a U.S. Department of Housing and Urban Development (HUD) office possible, the city needed to rehabilitate a downtown office building. To attain financing for the development of this office building, the City gained cooperation from the County government and the Board of Public Utilities (BPU). Together, these three governmental bodies provided a $1.5 million interest-free deposit (City: $500,000; County: $250,000; BPU: $750,000) to leverage a loan at 4% interest to allow for the development of the office building needed to house the HUD office.

To secure financing, the participating bank was provided with a 10-year interest free deposit beginning at $1.5 million and drawn down annually with the repayment of the principal. The bank was able to realize a 4% spread on the deposit and have a long-term deposit base to fund the loan. The reduction in the interest rate made the rehabilitation of the office building affordable.

With the location of the HUD office, a stable employment base of between 260 and 300 jobs was attracted to the City. This project demonstrates that even in the absence of an ongoing systematic linked deposit program, government bodies can still make occasional strategic linked deposits to achieve important economic development goals.

states pegged their linked deposit interest rates to U.S. Treasury securities, with one state at 300 basis points below the T-Bill rate, one state at 200 basis points below the T-Bill rate, one state at 300 basis points below the Treasury Bond rate, and one state at 105% of the T-Bill rate (offering discounts of up to 250 basis points based on job creation credits).

Nine states specified that linked deposit rates are tied to CD rates, seven at 300 basis points below comparable term CDs, one at 250 basis points below market, one at 200 basis points below market, and one state at one percent below market CD rates. One state had no set formula for determining rates for linked deposits but routinely negotiated rates of 250 basis points or more below market CD rates. One state administered a special linked deposit initiative that featured interest free deposits.

Among the cities that reported interest rate details, one links rates to Treasury bills. One city accepted 5% on linked deposits, four cities indicated that they made interest-free deposits, and one made deposits at 50 basis points below Treasury Bills.

Matching Interest Rates On Deposits To Loans

States and cities which make reduced rate deposits do so in order to enable special provisions for borrowers who receive the targeted loans. Usually these provisions include a lower interest rate, although at times they also include reduced fees, modified underwriting criteria, or other benefits.

Most states maintain a formula for matching discounted public deposit rates to discounts on the interest rate of loans leveraged by the linked deposit. Nine states required that the reduction from market rate interest earned on the deposit be matched by a similar reduction from the market rate on the type of loan leveraged. Four states set limits on the "spread" or difference between the deposit rate and the loan rate for linked deposits. This maximum "spread" ranged from 250 to 400 basis points.

Michigan used interest free deposits to secure interest free loans. In this case, loans were made from the state funds directly but banks were enticed to administer the loan application and review process with the incentive of using the unlent portion of interest free deposits to earn interest income. Montana bought Certificate of Deposits at a rate of 105% of Treasury Bills in order to leverage fixed rate mortgage loans and provide discounts of up to 250 basis points for loans resulting in job creation.

Five cities provided details on how deposit and loan rates are matched. Three of the cities specify a maximum interest rate spread. Akron, Ohio, provided for a 100 basis points interest rate spread (deposits at 5% and housing rehabilitation loans at 6%). Torrance, California, made interest free deposits to leverage interest free housing loans to the elderly and 4% housing loans to low- and moderate-income borrowers and Kansas City, Kansas, provided an interest free deposit allowing for 4% interest on the loan. Kansas City, Missouri, made deposits at Treasury Bill rates to leverage market rate loans in low- and moderate-income census tracts while Lansing discounted 50 basis points from Treasury Bill rates on its deposits in exchange for market rate loans with reduced application and servicing fees.

Terms of Deposits

In cases where the term of the linked loan matches the term of the public deposit, loan interest discounts are evenly matched by deposit discounts. However, longer-term loans can be a problem if the reduced rate public deposit used to leverage a reduced rate loan is outlived by the loan. In this case, the lending institution must, in effect, pick up the interest rate "subsidy" for the duration of the loan after which the reduced rate deposit is no longer available. In some cases, such as in large institutions where the linked loans are a very small percentage of the overall loan portfolio, the effect on a bank of making loans which are longer than the linked deposit may be negligible.

In general, linked deposit programs address this issue by limiting the required interest rate reduction on the loan to the duration of the deposit. However, banking regulators frown on the practice of funding long-term loans with short-term deposits. The problem of matching terms of deposits and loans is one major reason why most linked deposit programs focus on shorter-term business and agriculture loans rather than housing loans, and why shorter-term housing rehabilitation loans are more common than long-term mortgage loans.

Maximum deposit term limits among state programs ranged from one year to 20-years. Two states reported a maximum deposit term of one year. Two states had a maximum term of two years and one state was three years. One state's maximum was four years and three states had maximum terms of five years. Two states made one to two year deposits that could be renewed at the Treasurer's discretion. Three states did not indicate a maximum term for their linked deposits.

Among cities, deposit terms tend to be less clearly structured. Two cities had unusually long maximum terms on their linked deposits. Akron, Ohio, used Community Development Block Grant funds in its linked deposit to leverage home improvement loans for up to 20-years. The second longest deposit term cited was a ten year interest-free deposit made by Kansas City, Kansas, in exchange for financing of a major job retention project, with an annual reduction in the deposit linked to the repayment of the leveraged loan. Kansas City, Missouri, offers one year renewable deposits. The other cities either have no specified limits on the terms of deposits or did not provide detailed information.

A city or state's ability to make long-term loans is dependent on its overall fiscal condition. A fiscal crisis resulting in a very tight cash flow means that the city or state may have no funds to commit to multi-year certificates of deposit. The State of West Virginia, for example, discontinued its linked deposit program when it hit a severe financial crisis, and one other state is contemplating curtailing its program for the same reason.

CHART 5

FEATURES OF STATE LINKED DEPOSIT PROGRAMS

	INSTRUMENT & TERM	RATES: Deposit, Loan
MARYLAND	5-year CD	300 basis point reduction on CD and loan
KANSAS	1-year CD	300 basis point reduction on CD and loan
INDIANA	1-year CD (or less)	300 basis point reduction on CDs, 300 basis points spread
WEST VIRGINIA	2-year CD	300 basis point reduction on CD and loan
MICHIGAN		interest free deposits, loans; deposits = 120 percent of loan amount
TEXAS		200 basis point reduction on T. Bill, 400 basis points spread
WYOMING	5-year CD	300 basis point reduction on T. Bond, 300 basis point reduction on loan
IOWA		300 basis point reduction on T. Bill 400 basis points spread
ILLINOIS	1-2 yr. renewable CD	Flexible, gen. 250 basis points below market CD rates/loans
PENNSYLVANIA	5-year CD	100 basis points below mkt. on both loan, deposit
MONTANA	Up to 20 years	Up to 250 basis points reduction based on pay level of jobs created
OHIO	1-2 year CD	300 basis points below mkt. on deposits and loans
LOUISIANA	1-year CD	300 basis points reduction on deposits, loans
MAINE	2-year CD	200 basis point reduction on CD and loan
MISSOURI	1-year CD renewable	300 basis point reduction on CDs, loans

Application Procedure

In 12 of the 15 states reporting information on their application procedures, the application begins at the lending institution. In these states, borrowers interested in special linked deposit loans apply at state depository institutions. The institutions process the application and send it on to the state treasurer or the administering agency. The application generally requires documentation of eligibility such as the size of business or farm, income information, location, and the purpose of the loan. For business loans, several states require information and/or pledges regarding the number of jobs to be created or retained as a result of the loan. Several states have minimum guidelines on jobs created per unit of dollars deposited/loaned. The application is reviewed and approved by the State Treasurer. Guidelines on the rates and terms of linked deposits and loans determine the parameters but exact details are sometimes negotiated within the application process. In Michigan, where deposits are linked to loans to farmers suffering major crop loss, lenders must receive certification of the crop loss from the state's Agricultural Stabilization and Conservation Services before submitting the application to the State Financial Institutions Bureau and ultimately the State Treasurer.

In Texas, the State takes applications for linked deposit directly. Linked deposits in that state are used to leverage loans for alternative agricultural and horticultural crop production under a Department of Agriculture Program. Potential borrowers apply for loans through the Department of Agriculture which also provides technical assistance to the potential borrower. If applicants qualify, the application is sent to the Treasury which makes the deposit in a selected institution based upon the availability of funds.

In Maryland, where linked deposits are tied to high unemployment areas, applications generally originate from local government development agencies.

The State of Iowa also directly administers the business component of its linked deposit program through its economic development agency although many linked deposit applications come from banks. Other linked deposits are approved by the treasurer.

Five of the seven cities with linked deposit programs took applications through city development agencies. In all five of these cases deposits were linked to specific city programs. In Kansas City, Missouri, deposits are made

under an agreement that loans of a similar value will be made in targeted city neighborhoods. The bank, therefore, takes applications for these loans. Kansas City, Kansas, negotiated a linked deposit to finance a city initiative to retain a major employer and served as a broker between borrower and lender.

Monitoring Linked Deposits

State programs uniformly call for monitoring and review of linked deposits and usually specify remedies for non-performance. Monitoring is mandated at two levels: 1) monitoring of the bank's performance in executing the loan or loans with the remedy of withdrawing deposits or increasing interest payments on unlent deposits, and 2) monitoring the recipient of the loan to verify proper use of the loan and job creation or other results where relevant. Linked deposit statutes and program descriptions usually cover both types of monitoring in general terms leaving details open and up to staff or review committees.

In practice, most programs address the issue of monitoring primarily through attention to the application process. Applications are reviewed for eligibility, loan use, documentation of need, and employment or economic development commitment. Little monitoring is done after the linked deposit is made. Usually, the bank is required to submit an annual report but most states do not verify the information reported.

Monitoring the borrowers' performance can be the more difficult of the two types of monitoring. For programs which are primarily seeking to stimulate the private sector to make a certain type of loan, verification of the lending itself constitutes sufficient monitoring. When linked deposits are tied to specific standards for new jobs or other economic development measurement, monitoring becomes a greater problem. Most agencies charged with making linked deposits reported that they have very limited staff capacity to monitor the performance of individual loan recipients and therefore do minimal review. Exceptions include the State of Ohio, which regularly reviews employment data from firms to verify job creation results; and the State of Pennsylvania, which has 2-4 field examiners on staff who do regular site visits to all companies with linked loans.

In a couple of cases, enabling legislation establishes that false statements or improper use of the loans are a misdemeanor, providing a disincentive to noncompliance. Only two states, Ohio and Pennsylvania, require

documentation of employment figures and characteristics at the time of application which would provide a baseline for monitoring changes in employment over time.

For six of the seven cities which provided information, monitoring is an internal issue because the city itself either takes and approves applications or brokers the loan. The other city, Kansas City, Missouri, requires quarterly reporting of lending activity to verify that linked deposits are being used to fund loans in designated city neighborhoods. None of the city programs have numerical job creation requirements for their linked deposits.

Marketing

Most linked deposit programs utilize banks as the primary vehicle for marketing their programs. Several provide brochures to banks for distribution to potential borrowers. Potential borrowers then work with the bank to package a linked deposit request. In many cities and states, program staff also speak to chambers of commerce, local development groups, and other appropriate organizations to inform potential borrowers of the linked deposit program. Some also promote their programs through public service announcements and other press outlets.

Those programs which work with or through the state or city development agencies have a natural constituency and market the program through those agencies.

Some states market through eligible municipalities. The State of Maryland, for example, which targets high unemployment areas, depends upon the eligible cities to market the program for them.

Program Evaluation and Review

In general, states and cities with linked deposit programs have not performed evaluations of their impact and effectiveness. Only four states call for an annual review or annual reports of their linked deposit programs. Although a thorough evaluation of results was certainly not precluded, only the documentation of deposits made, loans and their uses and in one case jobs affected (as pledged at application) was required to be reported. A fifth state instituted a review board which could take on such a task.

None of the cities' ordinances or program descriptions indicate that any formal review or evaluation processes exist.

This lack of evaluation means that it is not possible to gather quantitative information about the actual economic impact of linked deposit programs, or to compare the relative effectiveness of different approaches by individual states and cities. Most important, it is impossible to compare the costs of a linked deposit program with its benefits. At the current scale of linked deposit programs in most cities or states, the total cost of the program, in both foregone interest and administrative/monitoring costs, is likely to be quite small relative to the total state revenues and the budget of the relevant governmental agencies and therefore possibly difficult to justify an impact study. Without an impact evaluation, however, it is impossible to evaluate whether a linked deposit program should be expanded or what changes could make it more effective. The lack of program evaluation also means that it is more likely that decisions to institute or continue a linked deposit program will be based on political, rather than economic considerations.

Officials in several cities expressed the desire to perform evaluations of their programs. Iowa is currently seeking funding to do so; and Pennsylvania is making plans to begin an evaluation. In Ohio, a cost benefit analysis was completed as a prior step to creating its linked deposit program.

Summary

States are much more likely to sponsor linked deposit programs than cities. There appear to be several reasons for this. First, city finance officers are more likely to be appointed officials while state treasurers tend to be elected officials. As a result, city finance officers are primarily financial managers while state treasurers have political agendas as well as broader policy mandates and authority. Second, states simply have much larger pools of funds, particularly longer-term funds with which to facilitate linked deposit initiatives. Third, states are more likely to look to their peers for policy initiatives to emulate. The first known linked deposit was Illinois' Specific Opportunity Program begun in 1969. The various state linked deposit programs share a number of features of this program. It is likely that state treasurers have borrowed from one another, possibly with the aid of national networks, while developing their own linked deposit programs. In fact, several treasurers indicated that Ohio's program was used as a model for their state's program. Cities would be more likely to be familiar with policy models more common at the municipal level.

Significant differences exist between state and municipal linked deposit programs. State programs tend to be more highly structured, much better funded, use general funds to leverage lending by private financial institutions, respond to a clearly delineated set of development needs, and involve broad participation by a number of financial institutions which generally participate in the application process. Municipal programs tend to be more specific in their lending focus and are often tied to a specific project or program, are likely to involve the participation of only one lending institution, are more likely to use CDBG or special program specific funds rather than general funds, and are more likely to use at least a portion of the deposits to actually fund loans.

While state linked deposit programs focus primarily on commercial lending to create or retain employment and on agricultural lending, cities primarily target housing, most commonly housing rehabilitation loans with their linked deposits. State programs share a number of common features while municipal programs tend to be more unique and varied in relation to both other cities and states.

State linked deposits commonly earn from 100 to 400 basis points below market rates on certificates of deposit or U.S. Treasury bills and are linked to loans with either a similarly discounted rate (from market loan rates) or with a ceiling rate of from 200 to 400 basis points above the rate earned on the linked deposit. Municipal linked deposits are widely varied from interest price to market rate with no real discernible pattern.

Linked deposit programs may pursue a wide range of economic development goals or focus more narrowly on specific critical areas. In some cases, linked deposits are used in a highly specific way to aid in the financing of an individual development project.

In addition to the general types of lending eligible for linked deposits (e.g., housing rehab, small business, and agriculture), specific definitions and guidelines for eligible lending are a common feature of linked deposit programs. In most programs, for instance, formulas on the number of jobs created per unit of dollars borrowed and/or definitions for eligibility based on the income or business size of loan recipients are spelled out in statutes or program guidelines.

Other specifics of process, documentation, and evaluation are common and essential elements of linked deposit programs. Programs tend to clearly define the process for applying and gaining approval for linked deposits, requirements for documenting that the lending project brings the promised results, and that such documentation is reviewed and evaluated. While it

is clear that most programs set guidelines and definitions, many administrators of public deposit programs indicated that resources are not available for a thorough verification and evaluation of results of either individual linked deposits or of the linked deposit programs in general. In some cases, these programs are relatively new and it would be difficult to evaluate their impact. In the long run, however, such objective documentation might be necessary to fully realize the potential of these programs.

IV. INCENTIVE PROGRAMS

Incentive deposit programs connect a financial institution's overall reinvestment or development lending performance to its access to public deposits. In contrast to linked deposits which seek to leverage particular loans, incentive programs seek to use public deposits to encourage financial institutions to engage in particular types of local lending or in overall lending patterns that serve the credit needs of the entire community. Several of the existing incentive programs were designed as broad anti-redlining, or community reinvestment statutes, or as programs that strengthen or supplement the federal Community Reinvestment Act and other anti-discrimination laws.

The 1977 federal Community Reinvestment Act (CRA) requires banks and savings institutions to serve the credit needs of their entire community, including low- and moderate-income segments of their community. The CRA is built on the concept that because depository institutions accept deposits from all segments of the community and have the privilege of government insurance to attract those deposits, these institutions have a duty to serve the credit needs of all segments of the community. A second initiative, the Home Mortgage Disclosure Act (HMDA), requires financial institutions in metropolitan areas to report data on their residential lending by census tract.

Incentive deposit programs build on the requirements of CRA by developing supportive policies on a local level. There are two types of incentive programs. **Screening** programs attempt to screen out from eligibility for public deposits those institutions with less than adequate reinvestment lending performance. Screening programs treat public deposits as a privilege that financial institutions must earn by meeting a minimum standard of reinvestment.

Reward programs go a step beyond screening programs. While screening programs focus on qualifying financial institutions for eligibility, reward programs actually link deposit awards to performance. In reward systems, financial institutions compete with one another on the basis of reinvestment lending performance for deposits from public institutions.

Both screening and reward programs rely heavily on the collection of data for evaluating the reinvestment performance of lending institutions. Just as the federal Home Mortgage Disclosure Act was created and passed as the initial step in uncovering bad lending patterns and as a prerequisite to reinvestment requirements, cities and states have included disclosure provisions as an integral component of incentive

deposit programs. In fact, the Chicago Municipal Depository Ordinance passed in 1974, became the model for the Home Mortgage Disclosure Act passed by Congress in 1975.

There are several key factors which incentive programs require:

1) The identification of local credit and development needs that form the basis for performance evaluation of financial institutions.

2) The collection of data that is useful in evaluating lending performance.

3) A meaningful analytical framework for the data that is collected.

4) A delineation of the authority and responsibility for carrying out these tasks of data collection, analysis, and evaluation.

5) A process for translating performance evaluation into the public deposit selection process.

Woodstock Institute's research found that cities and states are taking a wide range of approaches to implementing incentive deposit programs. Not all programs address all of the above factors and the methods of tackling each of them vary widely. Some of these efforts have experienced some success; others have been ineffective. Some programs have been considerably modified based on initial failures.

For example, two key elements of successful initiatives are the identification of appropriate disclosure requirements and procedures for analyzing data so that it can be useful for evaluating, rating, or ranking the performance of financial institutions. The approaches of states and cities to gathering and using disclosure data range from minimal involvement in evaluation to complex evaluation procedures.

In Chicago, for example, the City Comptroller collects disclosure data information on the geographic (census tract) location of savings and checking deposits and commercial, consumer, and residential loans. While the submission of the data itself has been required for eligibility as a depository for 16 years, the data has never been analyzed by the city or used to evaluate lending performance or guide depository selections.

Cleveland and Minneapolis, which have a similar history of data collection, have recently revised their process to take a more active approach. For years, Cleveland collected residential

lending data without any process for its review or analysis. In 1988, the City's ordinance was amended by a "Bank On Cleveland" ordinance to both expand disclosure requirements and to set up a process for its review. A reinvestment committee consisting of financial administrators, city council members, and community and banking industry representatives were empowered to analyze data, evaluate lending performance, and make recommendations on city depository decisions. In 1987, Minneapolis' disclosure requirements were actually scaled back to create a more manageable system of evaluating financial institutions.

At the other end of the spectrum, the State of Massachusetts has a reward program that relies upon a complex scoring system to determine eligibility and deposit awards. Banks are graded according to size and institution type classifications on a number of reinvestment and financial criteria. This program too, has met with criticism and has recently been reviewed for its effectiveness as a reinvestment tool.

CHART 6

INCENTIVE DEPOSIT PROGRAMS

	CITIES	
	Screen	Reward
Chicago, IL	x	
Minneapolis, MN	x	
Cleveland, OH	x	
Fresno, CA	x	
Pittsburgh, PA		x
Cincinnati, OH	x	
Boston, MA	x	x
San Diego, CA		x
New York City, NY	x	x
Dallas, TX	x	
Eugene, OR	Informal	
Milwaukee, WI	Proposed	

	STATES	
	Screen	Reward
Illinois	x	
Iowa	x	
Michigan	x	
Massachusetts		x
New Mexico	x	

These examples begin to illustrate the critical challenge of incentive-type public deposit programs: translating a straightforward concept to utilize public deposits to encourage and reward lending which is focused on local needs into a fair and effective system for actual depository selection. No current program has completely met this challenge; the practice of incentive deposits can best be described as in the 'trial-and-error' stage. The impact of existing programs depend on their scope and their success in addressing the key components identified above.

Existing Reinvestment Incentive Programs

Five states responding to the written survey--Illinois, Iowa, Massachusetts, Michigan, and New Mexico, reported having some form of anti-redlining provision in their laws or regulations governing public depositories. Two of these states, however, neither collect data nor perform any evaluations of the actual lending performance of potential public depositories. In Iowa and Michigan, potential depositories are required to provide lending disclosure data but this data itself is not evaluated and does not affect public deposit decisions.

Comprehensive disclosure requirements form a good basis for development of an incentive program but in most cases, the connection between disclosure and depository selection has not been made. Michigan's Anti-Redlining Act, for example, calls for the disclosure of residential application and lending data to monitor housing credit and to identify redlining. Financial institutions that fail to file disclosure reports become ineligible for public deposits. The Act does not provide, however, for basing public deposit decisions on performance evaluations that could be developed from the data collected. The activities of the Anti-Redlining Act are carried out by the State Department of Commerce, while deposit decisions are made by the State Treasurer. While the Department of Commerce notifies the Treasurer of non-compliant institutions (institutions that failed to file disclosure reports), no other collaboration is called for under the statute.

The Michigan Department of Commerce investigates complaints against lenders, collects and analyzes lending and application denial patterns throughout the state, focussing particularly on low- and moderate-income and minority areas. The Act also establishes community Voluntary Mortgage Review Boards and Community Investment Advisory Committees to identify and address credit problems in the state. These structures and activities provide a foundation for incorporating reinvestment and development considerations into the depository selection process but the connection has not yet been made.

Massachusetts is the only state which uses redlining disclosure data to implement an incentive program. The State has a reward system which scores banks on a number of criteria to determine deposit awards. Financial institutions are classified in five separate leagues by size and type of institution (three leagues for different sizes of commercial bank and two leagues for cooperative banks, savings and loans, and savings banks). Within leagues, the institutions compete for certificates of deposit and other time deposits. Among the criteria used for evaluating performance are: mortgage and home

improvement loans in low- and moderate-income census tracts; loans to small business; student loans; purchase of Massachusetts public agency securities; distribution of food stamps; and total in-state loans made.

Woodstock Institute's research identified ten cities which report having some form of an incentive program. Six of the cities reported having a reinvestment or anti-redlining program which is mandated by a municipal statute. These cities were Fresno, California; Chicago, Illinois; Cleveland, Ohio; Pittsburgh, Pennsylvania; Minneapolis, Minnesota; and Cincinnati, Ohio[1]. Three other cities have formal non-statutory policies that consider reinvestment as part of their public depository selection process. The City of Boston has implemented reinvestment provisions as part of its public deposit policy through an executive order and Dallas has done so through its Department of Taxation and Revenue's guidelines for depository bids. San Diego rewards small institutions with exemplary community lending performance with uncollateralized $100,000 deposits[2]. New York City has initiated a Community Banking Program through the promulgation of City Banking Commission rules.

In addition to these, Eugene, Oregon, indicated that it has informally conducted screening to insure that public depositories do not redline but had no statute or formal policy. Milwaukee, Wisconsin, has passed an ordinance to introduce social investment considerations in depository selection but has not worked out a specific program.

Three of the municipal programs, Pittsburgh, San Diego, and Boston, are reward programs. The others all are designed as screening programs.

These three reward program differ significantly in scope and process.

Pittsburgh has a 100-point scoring system in which 50 points correspond to a set of community development lending criteria. Banks in Pittsburgh compete with one another for scores that determine depository selection and deposit awards. Community lending performance is therefore designed to be a major factor in the actual level of deposit awards.

In 1990, the City of Boston initiated two separate incentive deposit programs: a city council ordinance and a program under

---

1. Hartford, Connecticut also has an anti-redlining ordinance with disclosure provisions but specific information was not available from city officials.

2. Complete information was not available on Cincinnati's program.

executive order. The executive order is the program that is currently being implemented. The order does not itself set up a scoring system but calls for the City Collector-Treasurer to analyze disclosure data and evaluate performance. The format for analysis proposed by the Collector-Treasurer is a scoring system that takes into account four sets of community lending and service criteria. The Collector-Treasurer is also authorized to freeze, withdraw or increase deposit awards, or negotiate with a bank in order to secure a desired level of performance. This authorizes the administration of a reward system that bases deposit awards upon performance evaluation scores. It also, however, provides an option of administering a screening system in which only particularly poor performance results in any action by the City to reduce or withhold deposits.

San Diego's program was initiated by the City Treasurer to make deposits which reward small institutions that are not eligible for larger deposits on the basis of their lending in low- and moderate-income census tracts.

The other seven city programs or initiatives carry features common to screening systems although some of these hold ambiguities similar to those in Boston. Chicago, Cleveland, and Fresno all require the signing of anti-redlining and/or affirmative reinvestment pledges but do not state that the actual distribution of deposit awards be contingent upon any level of performance. Of these, only Cleveland has empowered a reinvestment committee to make formal recommendations on depository selections. Conceivably, these recommendations could take the form of ranking or scoring banks, basing deposit distributions accordingly. However, the intent and the practice in Cleveland appear to be geared toward eliminating institutions with poor lending performance from receiving public deposits rather than rewarding institutions with awards commensurate with their performance.

Minneapolis also reviews the level of participation of financial institutions in city development programs to determine if their participation is adequate. Because the City assists in funding virtually all community-based development projects, this standard helps foster cooperation between financial institutions, community development organizations, and the City. Inadequate participation can result in a denial of depository status unless a satisfactory future commitment can be negotiated but the level of deposit awards themselves are not linked to performance.

Dallas has only recently undertaken a reinvestment incentive initiative. The fact that Dallas customarily selects only one financial institution for depository business, however, limits the program's ability to have a broad impact on reinvestment practice. The City is currently struggling to define disclosure

requirements that are both meaningful to its planning and development needs and can be obtained from depository institutions. Given that the city selects only one depository, its program might be characterized as a winner-take-all approach that is both a screening and a reward system.

New York City grades banks in four areas of lending and banking services and uses these grades in selecting depositories for the City's general funds. In addition, these grades must represent 10% of scoring for all city agency contract bids for banking services.

Cincinnati has established a committee on reinvestment to collect and analyze data and make recommendations on depository selections.

Disclosure Provisions And Data Analysis

Provisions for disclosure of lending data, reinvestment performance, and procedures for their analysis are critical components of incentive deposit programs. Without meaningful data collection and analysis, effective incentive programs cannot be developed or maintained.

Incentive-type deposit programs vary widely in the types of data required and the types of evaluation performed.

The State of Michigan's anti-redlining statute requires banks and savings institutions to report their HMDA loan origination data as well as the number of loan applications, loan denials, and the reasons for application denials.

The State of Massachusetts, which performs an extensive data analysis, collects disclosure data including loans to small businesses, student loans, state public entity bonds held, distribution of food stamps, and mortgage and home improvement loans made in census tracts with average family incomes of less than 85% of the state average, overall lending within the state, and investment holdings in U.S. Government Securities.

Seven cities--Boston, Chicago, Cleveland, Minneapolis, Pittsburgh, Cincinnati, and San Diego--have clearly defined disclosure data requirements. Dallas is in the process of defining disclosure requirements but is currently seeking zip code level data on residential and commercial loans. Fresno,

California, requires depositories to sign pledges to refrain from redlining and discriminatory lending practices, and prohibits deposits in institutions in violation of the federal Community Reinvestment Act. While the City's investment policy states that "treasury staff will continue to monitor related publications for any violation of this policy", no disclosure is required for monitoring reinvestment performance. Eugene, Oregon, indicated that staff informally review lending performance for redlining but did not indicate what data is used for this informal review. New York City is reviewing its disclosure requirements after completing its first annual review of disclosure information. San Diego reviews HMDA data of banks which compete for reward deposits.

The type of disclosure data required reflects each city's economic priorities. Of the nine cities with disclosure, all but one collect some type of specific residential lending data. One city, Chicago, requires HMDA reports to satisfy this requirement. Pittsburgh requires both HMDA data and the disclosure of mortgage loans that fit a special affordable home loan program criteria.[1] Performance in each of the HMDA and the special lending areas earn up to five points in Pittsburgh's scoring system.

Several cities modify HMDA requirements to obtain data more relevant to their needs. Cleveland requires residential lending data similar to HMDA data but reported by city statistical planning area rather than by census tract. Additionally, Cleveland requires data on loan applications (which becomes a feature of HMDA beginning with 1990 reporting). Boston requires disclosure of conventional and FHA/VA mortgage loans by neighborhood area as opposed to census tract (the city provides institutions with a tract-to-neighborhood conversion chart). Dallas is seeking to collect some form of residential loan data at the zip code level. Cincinnati requires loan application and lending data by race, gender, and neighborhood. New York collected information on bank participation in affordable housing lending in its first year but is now considering requiring HMDA data as well.

Seven cities require some form of disclosure of commercial lending. Chicago requires the reporting of commercial loans by census tract while Cleveland requires the same data to be reported by statistical planning area. Dallas indicated that it is seeking to craft disclosure requirements that include the reporting of commercial loans by zip code. Boston and Pittsburgh both request and score financial institutions on their loans to minority- and female-owned businesses. New York currently

---

1. The criteria for this program include: discounted interest rates, 30-year terms, 3%-5% down payment, no private mortgage insurance requirement, 95%-97% loan to value ratio, reduced closing cost and points, and 33%-38% debt to income ratios.

collects aggregate small business lending volume. Cincinnati collects application and loan data by race and gender.

Two cities (Chicago and Cleveland) also require the disclosure of an institution's sources of deposits by census tract. Deposit data can serve as a means of tracking the ratio of deposit business that is reinvested in particular communities. Boston indicated that such a ratio would be one of the methods employed in evaluating and scoring financial institutions for public depository eligibility.

Five cities, Minneapolis, Boston, Cleveland, Pittsburgh, and New York, required financial institutions to report on their participation in city development programs or agendas. Cleveland, for example, asks for the submission of information on the financial institution's lending activity in development initiatives that represent cooperative public/private partnerships involving government and community-based organizations.

Several individual cities require specific additional data. Chicago requires consumer loan disclosure by census tract. Boston requires student loan disclosure, affirmative action hiring data, information on services such as branch and ATM locations in minority neighborhoods, check cashing services for low-income residents, and bilingual services for customers. Pittsburgh requires the specific reporting of loans made to nonprofit community development organizations. New York requires data on branch and ATM locations, and banking services for low- and moderate-income residents.

Analysis of Disclosure Data

Only six cities and two states actually conduct any analysis of the disclosure data collected. The nature of this analysis varies significantly.

The common dilemma faced by program designers and administrators is the application of justifiable, objective standards for rating or evaluating the performance of financial institutions. Cities and states have tended to address this dilemma through one of two approaches. On the one hand, some programs set up a complex, multi-dimensional scoring system and examine the composite scores of institutions. This type of system is designed to reflect the numerous aspects of reinvestment performance and allow institutions to receive credit for differing types of programs and approaches. On the other hand, some programs have sought to simplify the process of analysis by evaluating financial institutions on a single measurement.

The first approach has the advantage of a more detailed evaluation structure. At the same time, program administrators acknowledge the lack of clear performance standards for these measurements means that scoring depends on judgments made by evaluators and is open to criticism that the process is too arbitrary. The second approach can be more objective but then limits the aspects of reinvestment which are evaluated and therefore limits the incentive impact of the program to those aspects.

The City of Pittsburgh is an example of an elaborate and detailed approach. Pittsburgh uses a 100 point scoring system to select public depositories and make deposit awards: 30 of the points are awarded on the basis of the price for depository services; 20 points are awarded for the reliability and efficiency of services received (banks are given the 20 points up front and can only lose points here through errors or unresponsiveness); and 50 of the 100 points are awarded on the basis of a set of community development considerations. Data and information is reviewed and scored in each of the following areas:

1) Mortgage and home improvement loans in low- and moderate-income neighborhoods. (5 points)

2) Participation in special affordable mortgage lending program. (5 points)

3) Commercial mortgages in low- and moderate-income neighborhoods. (5 points)

4) Construction and permanent financing to non-profit developers of newly constructed or renovated residential and commercial real estate. (5 points)

5) Participation in city programs to finance start-up and expansion of minority- and female-owned businesses. (5 points)

6) Participation in city and city agency redevelopment programs. (5 points)

7) Participation in and sponsorship of city and community organization sponsored events. (5 points)

8) Participation in community organizations to assess credit needs and to market relevant loan products to low- and moderate-income communities. (3 points)

9) Technical assistance provided to community organizations and to minority- and female-owned businesses. (3 points)

10) Contributions to community development philanthropic activity. (5 points)

11) Commercial loans to projects identified by the City Planning Department or the Urban Redevelopment Authority. (4 Points)

12) Purchase of municipal bonds issued by the City of Pittsburgh and its agencies. (4 points)

In scoring financial institutions according to this scale, Pittsburgh officials indicate that because there are no objective standards for scoring, financial institutions tend to be scored relative to other financial institutions. Institutions with the highest performance in a given category would receive the highest number of points, with others rated in relation to those. Evaluators must use their judgment in comparing institutions of different size and type.

In contrast, the City of Minneapolis is an example of a single criterion approach. The City's Community Development Agency reviews the participation of financial institutions in city development programs to determine whether that participation is adequate. Officials in Minneapolis believe that this simplified analysis gives institutions a clear picture of how they will be evaluated. The City will also make deposits in institutions which have been judged to have inadequate participation if they make specific commitments for future participation.

Other cities utilize one approach or a blending of approaches.

Only two other cities, Boston and New York, offered a formula for analyzing the collected disclosure data. In Boston, the Collector-Treasurer's proposed evaluation system scores four areas of a financial institution's activity: mortgage lending (33%); economic and housing development lending (33%); banking services (24%); and employment and promotion of minorities, women, Boston residents, and student loans (10%).

The evaluation procedures not yet implemented, state that, "category grades will be evaluated with an eye toward both comparative performances as well as the bank's capacity for contribution toward the city policy goals..." Each of the four areas has a set of components which are to be scored to arrive at a composite score for the institution, although it is not entirely clear how individual item scores will be determined.

New York City constructs a composite score for banks based on scoring in four areas: 1) affordable housing lending and

involvement; 2) small business lending; 3) branch and facility locations; and 4) service for low- and moderate-income customers. The best performers in each category score 100 points, with other institutions receiving scores relative to the top performer. Scores are given based on a combination of quantitative and qualitative considerations.

In Massachusetts, two sets of community lending and service activity are totaled for the linked deposit calculation. The calculation totals: 1) all loans to small business (maximum of 500 employees, $5 million in total assets $250,000 net before tax profit, and $2.5 million in net worth); 2) all student loans multiplied by five; 3) all Massachusetts public entities bonds held; 4) annual distribution of food stamps; and 5) all mortgage and home improvement loans made in low-income census tracts multiplied by five. These are then added to the institution's overall lending in the State, investment holdings of Massachusetts public entity securities, and investment holdings in U.S. Government securities. The final total is divided by the total in-state deposits held by the financial institution. Banks already holding public deposits document changes on both deposits and investments for a calculation of the institution's "maintenance of effort" to determine whether deposit awards will be increased or reduced.

While the State of Michigan does not base public deposit awards on reinvestment data, it does perform significant analysis of its required disclosure data. Data on loan origination, number of loan applications and denials, and the reasons for application denials is analyzed by the State Department of Commerce which produces an annual report detailing the lending and application denial activity of institutions throughout the state's metropolitan areas. Lending patterns in low- and moderate-income and minority census tracts are also outlined.

In Chicago, the City Comptroller publishes a report showing each depository applicant's lending by neighborhood and their percentage of lending within Chicago, compared to lending in the suburbs. This information is not used to make depository selections. Cleveland has a reinvestment committee that reviews disclosure data but the committee is not actively functioning and its methodology was not made clear.

Depository Selection and Decisionmaking

Of the 11 cities with formal disclosure requirements, only three, Pittsburgh, Minneapolis, and San Diego, have actually made public deposits based on the analysis of reinvestment data. In one of these, Pittsburgh, deposit awards are affected by perfor-

mance scores but the selection of the five institutions that serve as public depositories are not. Minneapolis bases awards on the single criterion of participation with public financing programs and San Diego's program is limited to a small portion of total public deposits.

Three cities with broad programs (Cincinnati, New York City, and Boston) are in the process of implementing their first round of deposit awards utilizing an analysis of reinvestment data. Three other cities (Cleveland, Dallas, and Milwaukee) are still designing or in the early stages of implementing their programs. Only in Chicago and Fresno are officials collecting disclosure data from financial institutions with no plans to analyze the data or use it for depository selection.

Of the five states with disclosure requirements, only Massachusetts uses its data to select depositories.

Most incentive deposit programs have a multi-tiered process for making actual depository selections and deposits. On a city level, this typically means that recommendations on depositories are made by a financial officer and/or reinvestment committee to the city council, which makes final decisions. The decisions are then implemented by the Treasurer who makes the actual deposits. On a state level, programs are implemented and decisions made entirely within the Treasurer's office. Any advisory committee or review committee would report to the Treasurer who makes final depository selections.

The only exception identified to this pattern is New York City, where all authority for decisionmaking is maintained within the City Banking Commission comprised of the Mayor, Comptroller, and Finance Commissioner.

This multi-level process means that the several implementation and decisionmaking steps must be coordinated to ensure that the overall process flows effectively and the program does not become bogged down in one particular part of the process. This requires that the specific responsibilities and authority for implementation be clear for every step of the process.

Where states and cities have experienced difficulties in the process of implementing their programs, it has been because the structure of committees, their authority, and responsibilities were not spelled out clearly enough at the outset of the program. In one city, this has led to disputes about the role and composition of the reinvestment committee. At least one other city has experienced political disputes between the different players in the process which might have been reduced through clearer lines of responsibility.

Program Evaluation

Little formal evaluation of incentive deposit programs has been performed by cities and states.

While most of the programs which collect disclosure data have made that data public, none have evaluated the ways in which the data has been used by the public or the extent to which constituencies which can make use of the data are aware of it.

To date, no city or state has performed a formal evaluation of the extent to which their programs have influenced overall lending policies. For the most part, programs are too new to have achieved any measurable impact. Given the constraints of staff and budget, however, it is unlikely that an individual city or state can perform an exhaustive analysis of community lending patterns before and after the implementation of an incentive program. Such an analysis would be complex to define, require extensive data gathering and analysis, and may not be cost-effective.

In several cities, administrators of public deposit programs which seek to reward financial institutions for reinvestment performance can cite specific examples of financial institutions which have made new lending commitments as a result of the program. Program officials have also cited benefits of increased consciousness of reinvestment issues among local banks, media attention to their programs, increased public awareness of reinvestment issues, and financial institution records as achievements of their programs.

Because most of the active incentive deposit programs are relatively new, and many are still working out program implementation difficulties, little additional data on program impact is available. As programs develop and mature, it will become important that additional documentation of impact be performed.

Summary

Cities are more likely to develop community reinvestment or anti-redlining incentive statutes or programs than states. This is because issues of redlining and community reinvestment tend to be focused at a local level, in terms of neighborhoods within a city, or a city in relation to its suburbs or surrounding area. Attention by citizens and community groups to these issues results in more impetus to local elected officials to enact measures to ensure local reinvestment.

Although they hold potential, the impact of this type of initiative has been mixed to date. In two of the states, anti-redlining statutes carry no real sanctions and require no disclosure to monitor compliance. In two others, data is collected but only one analyzes the data and neither link actual lending performance to depository eligibility. Only one state collects and analyzes lending disclosure data and gives scores to financial institutions on lending performance which are designed to determine actual deposit awards.

Five of the nine cities have had formal reinvestment provisions that generally were not monitored or enforced. Two of these cities required no disclosure to allow for monitoring. Three of these cities have long standing anti-redlining ordinances with loan disclosure provisions that were dormant and ineffective for years. While these ordinances pioneered and emphasized geographic loan disclosure, no real direction for use of the disclosure data was provided. Recently, two of those cities have redesigned these policies to incorporate public input and performance reviews into the actual depository selection process. Two other cities have enacted similar policies within the past year. These cities have also sought to overcome weaknesses of the earlier programs by institutionalizing loan performance review into the depository decision-making process. One of these cities, Pittsburgh, reports that this policy has already had a measurable effect on depository selections and local reinvestment commitments and performance. One city makes $100,000 deposits in several small banks and savings institutions as a reward for proven performance in lending in low- and moderate-income communities. One city is currently struggling with the disclosure issue in order to implement a recently developed reinvestment focus.

Incentive programs have the potential to affect a state or municipal reinvestment climate but must resolve a number of historically troublesome issues. These issues include: the collection of relevant and meaningful disclosure information to allow for monitoring reinvestment performance; the design of an analytic framework to evaluate performance; and clearly defined authority and responsibility for incorporating reinvestment performance evaluations into the selection of depositories and the awarding of deposits.

Those cities with active programs share some common elements. They have sought to involve city housing and economic development agencies. All five of the cities that reported having development, housing or planning agency involvement in public deposit selection had some form of incentive program. Financial officers, especially ones who are appointed, tend not to have either development agendas or expertise. The more active models also tend to be initiated by legislative or executive action though ordinances and executive orders do not themselves ensure successful implementation.

V. FEATURES OF PUBLIC DEPOSIT PRACTICE

Policies and procedures for investing or depositing public funds are determined by legislation, regulation, and the policies of treasurer or finance officers. Specific policies and practices may enhance or reduce the possibilities for reinvestment-oriented public deposit programs. Where reinvestment or linked deposit programs cannot be designed around existing practice, policies may need to be altered to accommodate the programs.

The following section outlines several components of overall public deposit practices, specific information on current practices gained from the written survey, and the relationship of these to reinvestment-oriented deposit programs.

Making Depository Selections And Decisions

The process for selecting depository institutions for public deposits and investments affects the potential for, and nature of, reinvestment-oriented deposit programs. In this decision making, there are significant differences between states and cities.

In 18 of 32 states, the treasurer was solely responsible for the selection of public depositories. Among the other 15 states surveyed, nine also involve another financial officer such as the comptroller, auditor, or a board of investments. The state legislature is involved in depository decisions in only one state and there is joined by the treasurer and a state board of deposits. Three states also involved the governor in depository policy. One state reported that the bid rating system itself controlled the decision-making. In another state, a special state depository board was in charge of selecting deposits.

In contrast, cities were far more likely to involve the legislative branch or chief executive in decision making. In 52 of the 101 cities surveyed, the city council was involved in the depository selection process. In 42 cities, mayors or city managers were involved in the depository selection process. In 87 out of the 99 cities responding, a financial officer was involved in depository selection process, either a treasurer, comptroller, finance director, or some combination of the three. In those cities where the mayor or city council made the final selection of depositories, financial officers would generally be responsible for submitting recommendations.

Only three cities indicated that any development agency staff or officer was involved in selecting depositories.

Two other cities indicated such persons were involved in depository selection under the various linked or reinvestment-oriented programs or process but not in overall selection. In all five cases where development experts or officers were involved in depository selections, the city had some form of a reinvestment-oriented public deposit initiative.

A key difference between cities and states is that at the state level treasurers tend to be elected officials with clear policy-making authority and interests while municipal treasurers and financial officers are more likely to be appointed officials with a narrower finance administration focus. This is a key factor in the difference between the origin of state linked deposit programs which tend to be treasurer initiated, and municipal programs which tend to be initiated by mayoral or city council activity, and most active when supported by housing and economic development expertise.

Interest Rate Requirements on Public Deposits

Interest rate requirements are an important consideration in the design of public deposit programs. Prudent money management requires a consideration of safety and return on deposits and investments. However, strict interest rate requirements, especially when statutorily mandated, can be a serious impediment to reinvestment-oriented public deposit programs. These programs often need below market rates on deposits to effectively create an incentive for significant reinvestment impact. In such cases, special enabling legislation is required to allow below-market deposits.

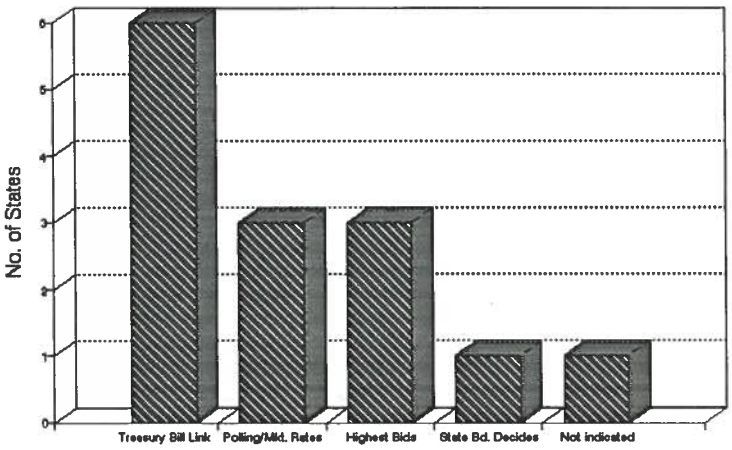
Formal interest rate requirements were much more common among state governments than among municipal governments. Fifteen of the 33 states which provided this information indicated a law or formal policy determines minimum acceptable interest rates. Only 17 of 67 cities responding indicated having such an ordinance or formal policy.

Those states with formal interest rate policies used several different standards to determine acceptable interest rates (see Chart 7). Six linked the minimum acceptable interest rate to U.S. Treasury Bills. Three states polled to determine competitive national or state interest rates and used those interest rates as a guideline in negotiating deposits. Three states required that highest bids (provided other safety and service considerations were met) form the basis for determining acceptable interest rates. One state indicated that minimum acceptable interest rates were set quarterly by a state board of deposits consisting of the governor, state treasurer, and

secretary of state but did not specify what criteria were used by the board. One state did not indicate how interest rates were determined.

CHART 7

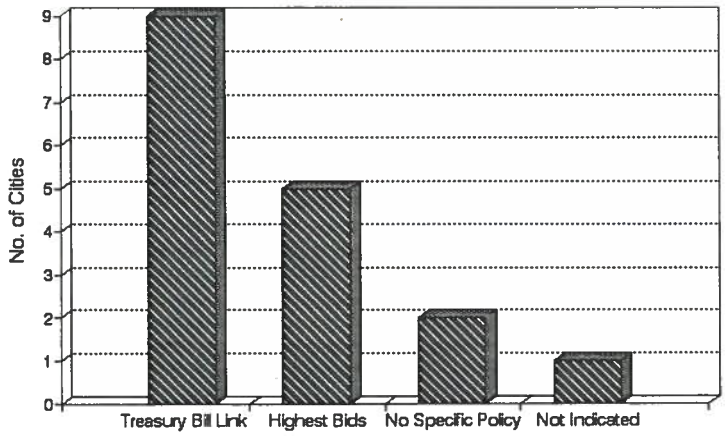
Determination of Minimum Acceptable Interest Rate, States



Among the 17 cities with formal interest rate requirements, (see Chart 8) nine tied the minimum acceptable rate to U.S. Treasury bills. Five cities indicated that highest bids (provided other safety and service considerations were met) constitute the minimum acceptable rate. Two cities merely required that deposits bear some interest but with no specific amount or formula.

CHART 8

Determination of Minimum Acceptable Interest Rate, Cities



Collateralization Requirements

Another factor that often has a bearing on the usefulness of a reinvestment-oriented deposit program is the amount and type of collateral required to secure public deposit funds. Because public deposits exceed the federal deposit insurance limit of $100,000, cities and states often seek to collateralize public deposits for protection in the event of financial institution failure. To collateralize a deposit, a financial institution pledges to hold specific types of securities for the state, usually U.S. Treasury securities.

The amount and types of collateral required by public depositors affect the number and types of institutions which can utilize public deposits. When a city or state demands collateral in excess of the funds deposited, public deposits are less attractive and sometimes not feasible for smaller financial institutions or an institution with a high proportion of its funds out in loans. This is particularly unfortunate because these more active lenders may be precisely the ones that incentive deposit programs seek to encourage. In some cases, flexibility in types of collateral which can be accepted helps to mitigate this problem.

Collateral requirements pose a particular problem for linked deposits. Because linked deposits require a specific loan or lending program as a condition of the deposit, accompanying collateralization requirements mean the institution must commit twice the funds deposited. The bank must use the deposit to buy, hold, and pledge the required securities as collateral and to fund the loans mandated by the linked deposit. While a large bank which holds a higher level of securities may be able to meet these requirements, a smaller community-based institution or an institution with a high proportion of loans may not be in a position to do so. In some cases, this means that those institutions most appropriate to particular linked deposit programs are not able to participate unless collateralization requirements are relaxed.

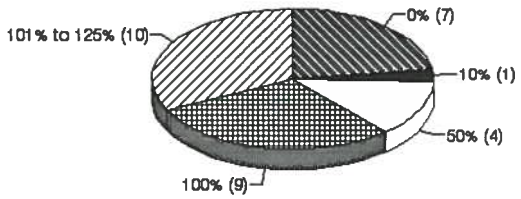
The following section presents information on current collateral requirements:

Amount Of Collateral Required

Twenty-nine states provided requested information about the amount of collateral required on public deposits. Collateralization levels ranged from none (seven states) to 120% of non-insured deposits (one state). Chart 9 gives the distribution of minimum collateral requirements. Slightly over 40% of the sample (12 states) reported that they require collateral of 50% or less, at least for some types of institutions and financial instruments.

CHART 9

Percentage of Collateral Required on Public Deposits -- States



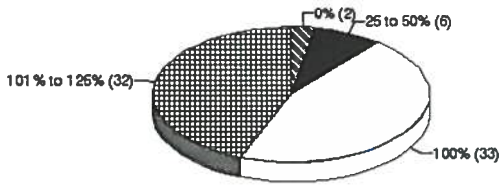
In some cases, minimum collateral requirements depend upon the type of financial institution holding the deposit or the type of security pledged as collateral. Three of the four states requiring less than 100% collateralization did so only for commercial banks and required at least 100% for savings institutions. The fourth state requiring 50% collateralization indicated that it sometimes asks for more if the treasurer deems it necessary.

Some states with 100% minimum collateral requirements require more than 100% on some deposits depending on the type of security pledged. For instance, Missouri indicated that most government securities were accepted at 100%, while mortgage-backed securities required 110%, and SBA securities required 125% collateralization. California requires 110% on government accepted securities and 150% on mortgage-related securities. One state indicated that the level of collateralization depended on the ratio of the percentage of the deposit to an institution's capital surplus.

Seventy-three cities provided information on collateralization requirements (see Chart 10). Here, in contrast to states, only 11% of respondents (eight cities) allow less than 100% collateralization on public deposits. Forty-three percent of respondents (32 cities) reported collateralization requirements greater than 100% of deposits. Twelve of these cities required between 101% and 105%, 18 required 110%, one required 120%, and the other required 125%.

CHART 10

Percentage of Collateral Required on Public Deposits -- Cities



Like states, cities often required varying levels of collateralization depending on the type of financial institution and security involved. For instance, cities in California, like the state itself, maintained differing collateral requirements depending upon the type of security pledged (110% on government and 150% on mortgage related securities). All but one of the cities, which required collateral but at minimum levels of less than 100%, made distinctions between types of institutions. In each case, commercial banks were required to provide collateral on less than 100% of deposit funds (all cities requiring 50%) while savings institutions were required to pledge securities on 100% or more of deposits held. In the only other city requiring less than 100% of collateral, 25% was accepted on deposit accounts while 102% was required on overnight repurchase agreements.

There was a difference of opinion between state and city officials, and bankers on the extent to which collateral requirements make public deposits less attractive. State and city officials interviewed, indicated that for standard public deposits, most banks are interested in receiving public deposits despite collateralization requirements. They reported that while bankers expressed a dissatisfaction with collateralization requirements for general deposits, most do not reject public deposits for that reason.

Bankers interviewed frequently indicated particular difficulties with collateral requirements for linked deposits. Some individual institutions including small

banks and credit unions, indicated they have not pursued public deposits because collateral requirements make the deposit financially unattractive to them. Generally, bankers reported that as an overall policy they were not interested in collateralized linked deposits but would consider them on a case-by-case basis. Some bankers, however, indicated they would be unlikely to accept any linked deposit that carried collateral requirements. Such deposits were less problematic for large banks doing a linked deposit loan that was small by their standards and represented an insignificant amount relative to their overall portfolio. The same tends to be true for banks with low loan-to-asset-ratios which more easily meet collateral requirements.

There were several notable exceptions to the common form of securing collateral requirements. At least three cities and one state maintain special collateral or insurance pools to secure deposits. The State of Wisconsin maintains a pool to insure $400,000 above the insurance limits for deposits by the state and cities within the State. This allows smaller banks to receive up to $500,000 in public deposits without having to tie up any of their securities in collateral pledges on public funds.

The State of Virginia and participating cities within the State also have a state collateral pool. Depository institutions pledge securities on 50% of the public deposit funds they hold and these securities are kept in a pool with the state treasurer. The pool is used to fully secure all state and participating city deposits.

The State of Indiana maintains a similar collateral pool, except that instead of pledging securities to the state pool, depository institutions pay assessments to maintain the pool which fully secures the public deposits.

While in these cases institutions share the risks of default by other institutions, the reduced collateralization requirements which result allow the institutions more flexibility in utilizing these deposits and greater income from the use of the funds.

Types Of Collateral Required

For states and cities alike, government securities were universally accepted as collateral on public deposits. In fact, for 13 of 23 states and for 51 of 74 cities, government securities constituted the only eligible type of collateral.

Of the 13 states that only accept government securities, three only accept securities of the U.S. Government or its agencies. Others accept various types of state, municipal, and other public authority securities. Ten states indicated that they accept non-governmental securities. Three of these accept only surety bonds as an alternative to government securities. The seven remaining states that responded accept various types of private bonds contingent on their rating.

Of the 51 cities that only accepted government securities, 12 restricted collateral to U.S. Government or agency securities. Twenty-three of 74 cities responding to the question indicated that various types of private bonds would be accepted as collateral contingent upon their ratings. Among the most common of the diverse types of non-governmental collateral accepted by cities were mortgages or mortgage-backed securities, banker acceptances, repurchase agreements, commercial paper, and highly rated corporate bonds.

Bankers interviewed indicated that the type of collateral required significantly affects their ability to accept and utilize public deposits, especially linked deposits. They indicated that broadening the eligible types of collateral could ameliorate some of their problems with collateralization and make them more willing to consider linked deposits.

Eligible Depository Institutions

States and cities have differing regulations specifying the types and sizes of institutions eligible for public deposits. Because different types and sizes of institutions can play different types of reinvestment roles, these regulations and restrictions have implications for the types and impact of reinvestment-oriented public deposit programs.

Information on the types of institutions considered eligible for public deposits as well as restrictions on size of institution is presented below:

Eligible Types of Institutions

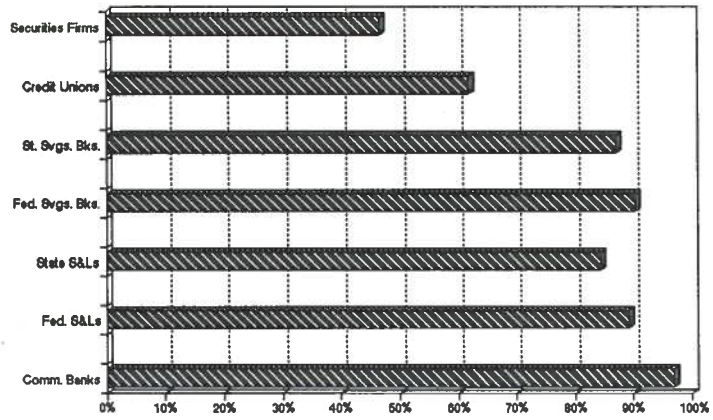
Commercial banks are considered eligible for public deposits in all states and virtually all cities that participated in this study (see Chart 11 and 12). Because these institutions have both the broadest lending authority and a

clear mandate through the Community Reinvestment Act to reinvest in low- and moderate-income communities, public deposit policies can play a significant role in rewarding strong reinvestment performance and encouraging targeting lending initiatives by commercial banks.

CHART 11

Eligible Depositories by Type

Cities

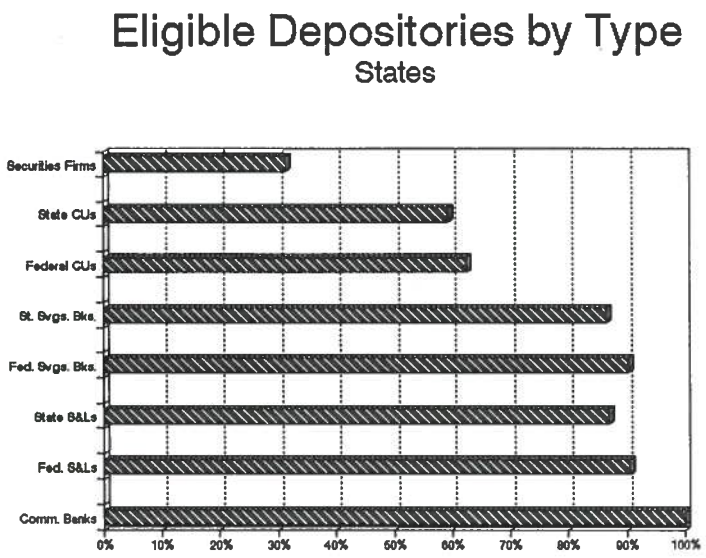


Almost all states and cities also consider state and federally chartered thrift institutions eligible for public deposits. These institutions are also subject to the Community Reinvestment Act. Unlike commercial banks, they have some restrictions on their commercial lending activity and do not have a history of small business lending experience. At the same time, these institutions offer additional opportunities for housing oriented reinvestment public deposit programs. Under the Savings and Loan bailout legislation, the Federal Home Loan Bank has funds available to help savings and loan associations to better serve the residential credit needs of low-income communities, providing both grant dollars and low interest loans to thrift institutions that develop special lending programs. States and cities have an opportunity to work with local savings and loans to leverage public deposits with these special opportunity programs.

Only a little over half the respondents (58% of states and 57% of cities) consider credit unions to be eligible depositories. In most cities, this prohibition was the result of state statute although in a few cities it was the result of municipal statute only. Because credit unions can

only lend to members as defined by their common bond, they are not subject to the Community Reinvestment Act. In addition, with the exception of state-chartered credit unions in a very few states, credit unions have regulatory restrictions on their commercial lending authority. Credit unions do offer federal deposit insurance equivalent to that offered by other insured depository institutions.

CHART 12



Some credit unions, however, can offer special opportunities for public deposits. There are now over 300 community development credit unions across the country which are chartered to serve low-income residents of specific communities. These credit unions provide an important source of credit, generally consumer lending and mortgage lending, and financial services to low-income populations with limited access to other financial institutions. Because of their limited access to large deposits, credit unions could benefit greatly from public deposits, particularly uncollateralized deposits.

Securities firms were least likely to be eligible depositories in the participating states and cities although approximately one-third of the states and one-half of the cities had no prohibition against the use of securities firms. The use of securities firms as depositories is perhaps the most clear example of cities and states using financial institutions or agents exclusively for maximizing their financial return. Although public deposits are generally not invested in equities, securities firms can sell investments that pay a higher return rate and they are

the financial intermediary used by the public sector to sell bonds. Securities firms, however, are not subject to the CRA, have no deposit gathering interest in low- and moderate-income communities, are usually not locally-owned, and do not invest in vehicles that directly benefit local economies. As a result, there is little opportunity to use reinvestment-oriented public deposits with these financial intermediaries.

Institution Size Restrictions

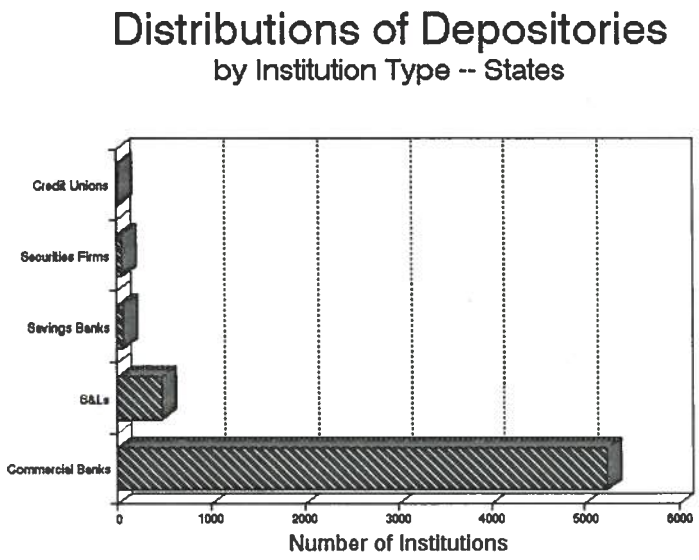
Most cities and states participating in our research do not have minimum asset size restrictions for public depository institutions. Only nine of the 47 cities responding to this question indicated that any minimum asset size was established for public depositories. Among these cities, minimum asset size restrictions ranged from a low of $500,000 (two cities) to a high of $4 billion. Other minimum asset sizes were: $2 million, $3 million, $5 million, $50 million, $75 million, $90 million, and $500 million. Of the 29 states responding to the question only two had established minimum asset size requirements. Of these, one state required $3 million in assets while the other required $3 billion.

Distribution Of Public Deposits

Having established the types of institutions that are eligible to be public depositories, the number and types of financial institutions actually used to keep public deposit and investment funds were researched.

Among states, commercial banks were the dominant institution for public deposits (see Chart 13). Nearly nine of ten (89.2%) institutions holding public deposit or investment funds were commercial banks. A total of 5,546 commercial banks served as public depositories for the 30 states responding to this question. Commercial banks comprised the majority of public depositories in all states but California which used more securities firms for public funds than any other type of institution. The next most common type of institution used as a public depository was savings and loan associations, 583 of which comprised 8.2% of the total depositories used by the 30 states. Other state depositories included 76 savings banks (1.3%), 22 credit unions (0.4%), 53 securities firms (0.9%), and two other types of financial institutions (0.03%).

CHART 13

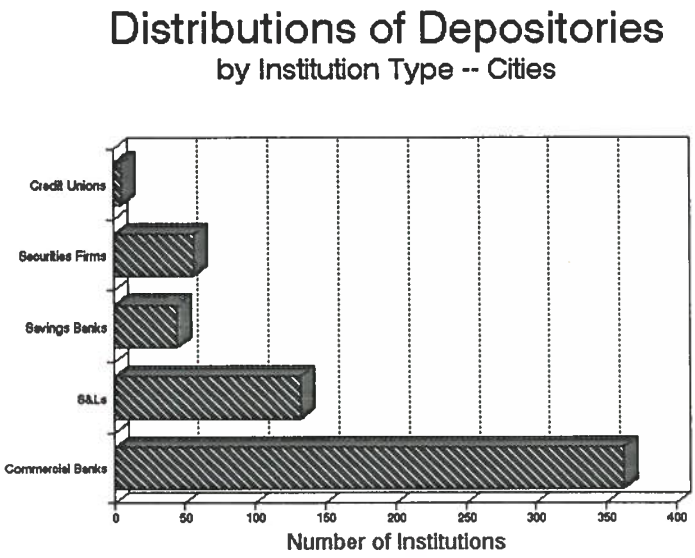


States differed significantly in the number of depositories used. The number of total institutions used as depositories for a single state ranged from a low of three to a high of 1,504. Three states used fewer than ten depositories, six used between 11 and 25, four states used between 26 and 50, four used between 51 and 100, six used between 101 and 200, four used between 201 and 500, two used between 501 and 1,000, and one state used more than 1,000 institutions as depositories.

Eight states used only commercial banks as depositories. Only seven states used credit unions for public depositories. Among these, Illinois, with ten credit union depositories, used more credit unions than any other state. Only six states used securities firms as public depositories led by California, which used 35, and Illinois, which used ten. Five states used savings banks as public depositories. Savings banks were most utilized as public depositories by Indiana, which had 57 savings banks serve as depositories. Twenty of the 30 states used one or more savings and loan associations as public depositories with Illinois having the greatest number of savings and loan depositories, with 225.

Commercial banks are also the most commonly used type of public depository institution among the 51 cities reporting (see Chart 14). Out of a total of 629 public depositories, 363 (57.7%) were commercial banks. In 42 of the 51 cities (82% of the sample) commercial banks made up the largest share of public depositories. In 14 cities (28% of the sample), all public depositories were commercial banks.

CHART 14



Savings and loan associations are the second most utilized type of public depository institution for cities. Savings and loans comprise just over one-fifth (21.1%) of all depository institutions. Savings and loan associations were the depository institution of preference in six cities, all located in the Western U.S. (four in California, one in Washington, and one in Arizona). In 28 cities, however, no savings and loan associations served as public depositories.

Securities firms constitute the third most commonly used type of public depository, making up 9.1% of all depositories. In three cities, there were more securities firms handling public funds than any other type of financial institution. Thirty-four cities, however, did not use any securities firms as public depositories.

Types of Deposits And Investments

The types of deposit and investment instruments used by state and municipal governments is important to the design of development oriented programs. Most linked deposit programs use certificates of deposit as the deposit base for development loans. Reinvestment-oriented screening or reward systems can utilize all types of banking deposits as incentives for reinvestment activity. The more desirable the deposit or investment is to the financial institution, however, the stronger the incentive to development lending will be. The data reported below on the distribution of public funds by type of financial instrument represent

choices that are made and could, to some extent, be changed to better suit development-oriented goals.

The survey data on the distribution of public funds by financial instrument show that while there are certain instruments that are more commonly used than others, overall, there are significant differences among the states and cities in terms of the distribution of public funds between the various types of deposits and investments.

Distribution Of State Funds

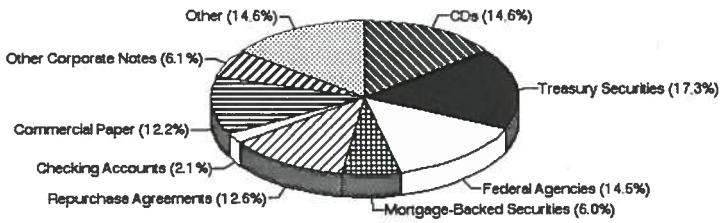
The 30 states reporting the distribution of their deposits by type of financial instrument reported a total investment portfolio of $78.7 billion. Certificates of deposit account for the largest single type of instrument with $11.5 billion, or 14.6% of total invested dollars for the 30 states combined. Though the use of certificates of deposit did vary between states, most states surveyed made significant use of CDs (see Chart 15).

The volume of deposits currently in CDs is particularly important because CDs are the common vehicle for linked deposits. Those states with significant levels of CDs can most easily institute or expand linked deposit activities. Those with minimal levels of CDs might need to shift funds from other types of instruments in order to establish a linked deposit program.

There is, however, substantial potential for linked deposit programs within the existing volume of CDs held by states. If all states reporting committed 10% of all their CDs funds to linked deposits, an average of $383.3 million annually per state would be made available to leverage development lending this amount would represent only 1.5% of total state funds available for deposit and investment in these states.

CHART 15

Distribution of State Funds



United States Treasury Bonds, Bills and Notes made up 3.5%, 5.7%, and 8.1% of total state funds respectively, collectively accounting for 17.3% of total state funds. In addition, another 14.5% of total state funds were invested in other obligations of various federal government agencies.[1] Together these various federal securities constitute nearly one-third of all deposited and invested public funds (31.8%). Mortgage-backed securities, the vast majority of which are issued by federal or quasi-public federal entities, constituted an additional 6% of all state funds, bringing the percentage of total state dollars invested in these securities to 37.8%.

Taken as a group, U.S. Treasury and Federal Agency securities are the most widely used instrument for state funds. Only four states placed no funds in these instruments, while another placed less than one percent in them. Treasury Bills carry short-terms of one year or less, similar to term CDs. Treasury notes carry terms of one to ten years while Treasury Bonds carry terms of ten years or more. Mortgage-Backed Securities are long-term instruments which often carry terms of 15 to 30 years. Because they are all actively traded in secondary markets, however, these are liquid investments which are not necessarily held for their full-term. To the extent that these investments are held for terms similar to CDs, they represent potential linked deposit funds.

Repurchase agreements are a widely used public deposit instrument representing $9.9 billion, or 12.6% of total funds deposited and invested by the 30 states. Repurchase agreements are actually short-term (usually overnight) purchases of treasury securities which are bought back the next day by the bank or securities firm. Repurchase agreements allow governments to gain income from short-term funds as an alternative to placing them in non-interest bearing checking accounts or taking potential losses as a result of being forced to sell longer-term investments off to gain cash. Repurchase agreements are attractive to financial institutions because they provide them a source of liquid cash. To the extent that repurchase agreements are desirable to banks, they are useful to an incentive program approach. Because of their term, however, they are not useful in linked deposit programs.

The percentage of state funds placed in repurchase agreements varied widely among the 30 states. The median

---

1. The total for federal agency securities includes some Treasury bonds, bills, and notes that were reported together in aggregate.

percentage of funds in repurchase agreements for the 30 states was 9.3%.

Bankers acceptances account for $4.2 billion of state funds, 5.4% of total funds for the 30 states. Bankers acceptances are basically IOUs that serve a function similar to repurchase agreements, but usually with longer-terms. The percentage of total state funds in bankers acceptances is somewhat misleading in that bankers acceptances are not widely used among the 30 states. In fact, five states account for the vast majority of funds invested in bankers acceptances. Twenty-three states had no funds in bankers acceptances while one other state had less than one percent.

Commercial paper or short-term debt instruments of highly rated private corporations accounted for $9.6 billion in state funds, 12.2% of the total funds of the 30 states. While commercial paper may carry terms of up to one year, they often carry shorter-terms of two or three months. The use of commercial paper is fairly evenly mixed between those which barely use the instrument and those with substantial use of it. A significant number of states are prohibited by law from investing in commercial paper.

Other corporate notes and bonds with longer-terms made up $4.8 billion or 6.1% of the 30 states' funds. Interestingly, seven states which accept only government securities as collateral on deposits make direct investments in these private securities. Twenty-four states had no funds invested in corporate obligations while one other had less than one percent invested in them. The other five states reported shares of total funds in corporate securities ranging from 7-30%. In many states, private securities are statutorily prohibited investments.

Only 2% of all funds of the 30 states were held in checking accounts ($1.5 billion). The highest percentage of funds that any state had in checking accounts was 11%. Eight states had no funds in checking accounts, 11 states had a fraction of one percent, and ten states had between one percent and 10% of their funds in checking accounts. The median percentage of funds held in checking accounts among the 30 states was .05%. While not useful to linked deposit programs, checking accounts may represent desirable business to banks within the framework of an incentive program. Sometimes states and cities offer checking account business to banks in exchange for other banking services.

Savings accounts accounted for only 0.5% of the states' funds ($405 million). Savings accounts tend to carry relatively low rates, particularly on shorter-term funds, a

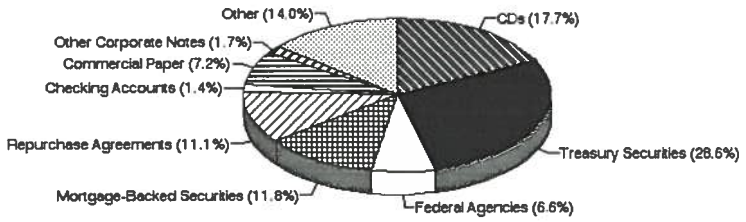
likely disincentive to their use by public entities. Twenty-seven of the 30 states had no funds in savings accounts, two states had a fraction of a percent and one state had 18% of its funds in savings accounts. The remaining 8.7% of state funds were deposited or invested in a variety of other types of instruments.

Distribution of Municipal Funds

Collectively, the 64 cities reporting data on their deposits held a total of $11.5 billion in various financial instruments (see Chart 16).

CHART 16

Distribution of Municipal Funds



As with the states, combined U.S. Treasury and various federal agency securities are the most common types of investments for municipal governments. Cities invested an even greater portion of funds in these securities than states, however. Combined U.S. securities accounted for 35.2% of all municipal funds (14.9% Treasury notes, 13.2% Treasury bills, 0.5% Treasury bonds, 6.6% other federal agency securities), compared to 31.8% for states. Mortgage-backed securities accounted for another 11.8% of the 64 cities' total funds, bringing the percentage of total funds in these government related securities to 47%.

Among cities, the longer-term Treasury bonds accounted for a smaller proportion of total investments than for states (0.5% for cities, 3.5% for states), an indication that

cities have fewer long-term funds available than states. Conversely, cities held a significantly greater share of their funds in both Treasury notes (14.9% for cities, 8.1% for states) and Treasury bills (13.2% for cities, 5.7% for states). This was not the case, however, with mortgage-backed securities. Cities put 11.8% of their funds into mortgage-backed securities compared to 6% for states. As noted above, mortgage-backed securities are actively traded on the secondary market and can be held for short- or long-terms.

Certificates of deposit accounted for 17.7% of all municipal funds, making CDs the single most commonly used instrument among the 64 cities. A 10% allocation of municipal CDs to linked deposits, distributed equally among the 64 cities, would produce $31.7 million per city per year in leveraged development lending. Yet, this allocation would represent less than 2% of total municipal funds.

The use of CDs varies significantly between the cities. Percentages ranged from 0% for six cities and less than one percent for another 11 cities to a high of 100% for one city. Ten cities placed 75% or more of their total funds in CDs.

Repurchase agreements constituted the next highest portion of municipal funds, accounting for 11.2% of all funds, only slightly less than the percentage for states (12.2%). Again, cities' use of this instrument varied greatly.

Private corporation securities, commercial paper and corporate notes, accounted for 8.9% of total municipal funds. Seven percent of municipal funds were held in short-term commercial paper (one year or less), while 2% was placed in intermediate-term corporate notes (1-10 years). Cities invested significantly less of their funds in these private corporate securities than did states. Five cities which do not accept private securities as collateral on their deposits invested directly in private corporate securities.

Use of commercial paper was very limited among the 64 cities with only one in four cities (16) using them at all. For all cities combined, however, commercial paper constituted 7.2% of all municipal deposits.

Similarly, 58 cities reported no investment in corporate notes. Collectively, corporate notes accounted for 1.8% of all municipal funds.

Investments in special state investment pools constituted 5.2% of total municipal funds. A total of 18 cities in 12 different states reported having funds placed in state investment pools. While 46 cities, (72% of those reporting) reported no investments through their state, such investments were quite popular with a small set of the cities. Six cities invested between one percent and 10% in their state's fund, five cities invested between 11% and 25%, four cities invested between 26% and 50%, one city invested between 51% and 75%, and two cities invested more than 75% of their total funds in their state's investment fund.

The remainder of municipal funds were distributed among the various instruments in the following manner: checking accounts (1.4%), state and municipal bonds (1.4%), savings accounts (0.8%), and various other investments (1.4%).

Among these, only checking accounts were widely used among the cities. They generally accounted for very small portions of total municipal funds. Only 13 cities reported having no money in checking accounts while five cities placed more than 10% in checking accounts.

VI. CONCLUSIONS AND RECOMMENDATIONS

This report has shown that in addition to keeping public funds safe and earning interest income on those funds, treasurers and finance officers in a number of cities and states across the country are attempting to serve an additional public purpose by using public funds to promote or leverage lending by private financial institutions in targeted areas of economic need. The 35 reinvestment-oriented public deposit programs described in this report demonstrate a range of approaches and varying degrees of success and impact. Taken as a whole, they illustrate the potential impact of such programs as well as many of the issues and problems that should be addressed to increase their effectiveness.

Reinvestment-oriented public deposit programs enable financial institutions to engage in low cost financing in key areas of economic interest to a state or city and encourage private financial institutions to better serve important but underserved credit markets. They also serve as an additional level of support for federal Community Reinvestment Act requirements. These initiatives do not put public funds at any additional risk because loans are underwritten by the financial institution itself and public deposits under these initiatives must meet the same collateral requirements as other public deposit funds.

There are two types of approaches to reinvestment-oriented public deposit programs: incentive programs, which take the reinvestment record of financial institutions into account when selecting depositories for public funds; and linked deposits which link individual deposits usually at below market interest, to specific loans or lending programs. While many cities and states have taken one or the other of these approaches, they are not mutually exclusive but can complement one another within an overall public deposit policy.

One major advantage of public deposit programs is their ability to utilize public capital without actually spending that capital. While this means that public deposit programs can be a cost-effective approach to promoting needed community investment, these programs do incur some costs. Depending upon the approach, this cost ranges from increased administrative costs (for analyzing disclosure data or reviewing and monitoring lending performance for incentive programs) to lost interest earnings (on reduced rate deposits for linked deposit programs). For a full picture of the cost effectiveness of public deposit initiatives, these costs must be weighed against any increased tax revenues created by the loan activity as well as the program costs and additional risks that would be incurred if the targeted lending were undertaken directly by the government entity.

Our specific conclusions and recommendations for each of the two types of reinvestment-oriented public deposit programs follow.

Incentive Programs

Incentive programs of various types have been advanced in at least ten cities and five states across the country.

While the framework of incentive public deposit programs holds promise for broad influence over reinvestment policies, to date, existing incentive programs have a history of being underutilized and ineffective. There appear to be a set of identifiable issues that have been responsible for this lack of success.

Chief among these are the difficulties of data collection and analysis. In order to make the performance evaluations which are the heart of such initiatives, information must be collected and analyzed in a meaningful way. Incentive programs have historically failed either by not collecting information necessary to make such evaluations or by failing to develop a framework for evaluating the data which has been collected. Obviously, in cases where no information is collected, there is no possibility for making meaningful depository selections based on reinvestment criteria. Developing a meaningful and objective method for analyzing data, however, has also proven to be very difficult.

The first problem is that there are no established or recognized standards for what constitutes adequate reinvestment performance. The only formal evaluation of reinvestment effort and performance is that performed by financial institution regulators as mandated by the Community Reinvestment Act. Until July, 1990, CRA ratings were not publicly available and regulators gave virtually all institutions acceptable ratings. In most CRA challenges, community groups have established the inadequate performance of banks on a case-by-case basis, analyzing lending patterns, loan products, and other factors. While creative and effective, these efforts have not established standards or norms for evaluating reinvestment performance in general. Differences in the size, type, specialization, and location of institutions make establishing such norms an elusive undertaking.

One approach to the lack of objective standards has been to rate banks in a number of areas and score or rank them in relation to one another or to top performers in each area. While this provides a relative standard, if all institutions are poor

performers the standards are set quite low and differences in the nature of the institutions are not taken into account. An additional evaluation problem has been that city or state governments have tended to assign the task of evaluation to a finance officer who is often unfamiliar with community development issues and is more interested in fiduciary matters than development policy. Sometimes legislatures provide policy mandates without providing adequate resources to carry them out. Without input from development agencies or adequate resources, it is often difficult for financial officers to effectively administer an incentive deposits program.

Another data collection pitfall of the incentive program approach is the specification of disclosure data requirements. For example, a city requires geographic commercial loan disclosure but does not specify whether to report the location of the end use of the loan or a downtown main office. It may not be clear whether snapshot portfolios or annual activity should be reported, or if annual activity whether it should be calendar year or fiscal year. There are numerous such details that must be attended to when defining disclosure data requirements to ensure useful and consistent data.

The other balance necessary is that disclosure data requirements that are too stringent may be a disincentive to participation for some financial institutions, particularly smaller ones. If this happens, the idea of public deposits serving as an incentive to increase lending or improve reinvestment performance has been contradicted.

Despite these difficulties, disclosure remains an essential component of any incentive deposit program. Without federal disclosure requirements (which have recently been expanded by Congress), the Community Reinvestment Act would have been nearly impossible to enforce. The task of collecting and using disclosure data, however, must be tackled clearly and with great precision.

An additional difficulty with existing incentive programs is that each one has, for the most part, been designed independently. No one successful model has guided the initiation of other programs. Each state or city has therefore had to reinvent the wheel to establish its program.

Finally, a number of programs have found themselves bogged down in the process of implementation. This has been a particular problem when: 1) there is no clear authority for implementing the program; 2) there is no political consensus for the program (for example, between the mayor, the Treasurer, and public interest groups); or 3) the mandated process for implementation has been too unwieldy or involved too many layers of decisionmaking.

While implementation of incentive deposit programs has proven problematic, there is significant interest among cities and states in developing successful approaches to incentive deposits. Many programs are being modified to address earlier difficulties. A new generation of incentive deposit programs, most of which are too new to evaluate, are being established. This research has, however, identified a number of steps detailed below which should be taken by incentive programs to avoid the failures of the past.

Linked Deposit Programs

Linked deposit programs have had a much stabler and more active history than the incentive programs. The first known linked deposit program was started in Illinois in 1969. Since the implementation of this first program, as many as 15 states have implemented linked deposit programs, several in the past five years. These programs vary in their goals and size but several have maintained significant levels of activity over time. Seven cities have also instituted linked deposit programs. Because they are more limited in scope and in purpose than incentive deposit programs, linked deposit programs have had fewer problems in their implementation.

State linked deposit programs often deposit tens or hundreds of millions of dollars in linked deposits, leveraging similar amounts in below-market rate loans. There are two basic approaches to linked deposit programs. The first is to generally stimulate activity in important sectors of the state's economy through providing lower cost financing to those sectors without any specific link to job creation or retention. The other is to link deposits to loans that will result in the creation or retention of a specific number of jobs per amount deposited. Both approaches are worthwhile but represent their own set of problems.

Programs that wish to impact or stimulate strategic areas of a state's economy without a specific quantifiable result seem to work well when there is political consensus on the importance of those goals. In the absence of such a consensus, they are open to criticism that the program is merely reducing interest revenues for the state. Programs that link deposits to loans that result in the retention or creation of a set number of jobs, theoretically have the evidence to prove their benefit as weighed against the costs of foregone interest. However, though the information is incomplete and sketchy, it appears that monitoring of job creation results is generally lax and there are no known examples of an actual impact study for any linked deposit program. The one such impact study that has been done was by

the State of Ohio, prior to the enactment of its linked deposit statute. The difficulty in closely monitoring impacts and the relative lack of hard documentation of results could be a factor in a public official's decision to initiate such a program or to be aggressive in the administration of one that already exists.

The most active and successful linked deposit programs share a number of characteristics. First, they are state programs, often in states with elected treasurers. Elected officials appear to be more interested in pursuing public policy goals and agendas than appointed finance officers who tend to operate under a more restricted money management mandate.

Second, most states with linked deposits have enabling legislation or clear constitutional authority that allows the Treasurer to set deposit policy and to make below-market deposits to pursue economic goals.

Third, unlike the incentive programs which have had to struggle with data collection and analysis, these linked deposit programs are able to set up a clear set of deposit guidelines, eligibility criteria, and review applications in order to make a quick determination on a linked deposit. In fact, in most states, banks check for eligibility and documentation before submitting proposals to the state.

Fourth, active linked deposit programs have effective marketing, usually relying upon the banking community, chambers of commerce, and other business and agricultural trade groups to market the program. When linked deposits are affiliated with other state development programs, other agencies such as departments of agriculture or economic development market the program through referrals.

Linked deposit programs also face a number of common problems. These include:

- The programs are vulnerable to overall fiscal pressures in the state. At least two states have recently suspended their linked deposit programs due to fiscal crisis. When a state faces a shortfall of funds or a possible deficit, there is little or no opportunity to place linked certificates of deposit for any length of time that would enable a bank to make development loans.

- The types of lending possible with linked deposits are limited by the terms of deposit which can be offered by the state or city government. Most states use one or two year certificates of deposit renewable to a maximum of four to seven years. While deposits with these

terms are useful for many business and agricultural loans, they are less useful for leveraging housing loans or other loans which carry much longer-terms. The use of public deposits as one piece of a multi-level financing package, however, can make them appropriate for a wide variety of loan purposes.

- Collateral requirements can be an impediment to the use of linked deposits for some banks. Collateral requirements of more than 100%, especially when restricted to U.S. Treasury securities, means that banks have an unbalanced mix of two assets matched to one liability. This is particularly a problem for banks that have high loan-to-deposit levels. Given the current bank insurance environment, local governments have a legitimate concern for the protection of their deposited funds. Flexible approaches which recognize both a reasonable need for security on the part of government and the benefits which can accrue from linked deposits need to be pursued.

- Although linked deposit programs are relatively widespread at the state level, in most states even active programs utilize only a very small percentage of total public deposits. The lack of documented evidence of the benefits of current programs, however, makes it more difficult to argue for their expansion or for changes in their terms, such as interest rate reductions or flexibility in collateral requirements which could expand their impact.

- While some states and cities coordinate linked deposit efforts with state development agency programs, most do not. Such coordination could maximize the effectiveness of other government development efforts as well as simplify some of the monitoring needed and provide additional staff resources for the linked deposit program.

Recommendations

There are a number of possible strategies, actions, and further research which can be undertaken to address the problems that have been identified in this exploration of public deposit programs as well as to encourage the more widespread use of this development tool among states and cities. Some of these apply specifically to incentive programs, others to linked deposit programs, and others to both types of reinvestment-oriented public deposit programs.

Incentive Programs

Improve performance evaluations and standards. In most states and cities with incentive programs, policymakers and administrators are still seeking a system for evaluating financial institutions which is both comprehensive enough to reflect various components of reinvestment performance and the differences between types of financial institutions and simple enough to be easily administered. To date, no ideal model is in place. The lessons learned from existing programs lead to several recommendations for designing a evaluation system:

1. Include easily measured, objective standards. The specific standards may be based on the specific credit needs of the individual city or state.

2. Designate minimum standards for eligibility of an institution for public deposits. Minimum standards which are understood by financial institutions are an important basis for both screening and reward systems for deposits.

3. Involve persons with community development and reinvestment expertise in the development of standards. This should include persons from both outside and inside of government.

4. Allow future reinvestment commitments by a financial institution performance to be considered in determining eligibility for public deposits. While actual performance on those commitments should be monitored, allowing negotiations on future commitments enhances the incentive effect of the deposit selection process.

Explore the use of the new Community Reinvestment Act ratings for qualifying financial institutions for public deposits. Provisions of the comprehensive savings and loan bailout legislation significantly strengthened the reporting requirements and evaluation mechanism for CRA examinations and ratings. Disclosure data has been expanded for 1990 to include information on race of mortgage applicants and on applications approved or rejected. All CRA ratings based on exams performed after July 1, 1990, are publicly available. The rating system has been changed with the intent of providing more meaningful evaluations of actual performance.

These changes may result in CRA ratings which will provide useful standards for evaluating the reinvestment performance of individual financial institutions.

Results of examinations to date, however, are mixed. As of March 27, 1991, 89% of all financial institutions examined since July 1990 received either an "outstanding" or "satisfactory" rating. Evaluation standards do not yet appear to be fully consistent across regulatory agencies or regions.

But CRA examinations, if well utilized by regulators, could provide cities and states with a straightforward, external evaluation which could greatly simplify the task of screening financial institutions. Officials working with public deposit programs should monitor the CRA ratings of local financial institutions to determine whether they can be utilized in a screening process. If examinations under the new evaluation procedures prove to be inadequate for differentiating the performance of financial institutions, local officials should encourage banking regulators to more stringently evaluate CRA compliance.

Improve data collection and analysis. As discussed previously, data collection is a balance between collecting sufficient information to be useful while not unnecessarily burdening financial institutions or accumulating more information than can be analyzed by public deposit decisionmakers. Specific recommendations in achieving this balance in design of public deposit programs include:

1. Targeted areas of credit need should be clearly articulated so that disclosure data requirements can flow directly from them.

2. Terms and definitions for disclosure should be clearly specified and defined so that information received from different financial institutions is comparable.

3. Utilize already-required disclosure data where possible. New federal reporting requirements effective for 1990 provide additional data on loan applications and other information which will be useful to local officials and may reduce any additional reporting requirements necessary.

4. Don't collect more data than can be evaluated in the public deposit decisionmaking process.

5. Keep reporting requirements simple enough so that financial institutions, particularly smaller institutions, are not discouraged from applying for public deposits. If public deposits become unattractive to many institutions because of reporting requirements, the incentive value of the program will be lost.

Make information and data disclosed by financial institutions available to the public. Public access to disclosure data allows community organizations and public interest groups to also analyze the data and strengthens the incentive impact of the disclosure.

Where they are not currently eligible, the expansion of public deposits to additional types of financial institutions, such as community development credit unions, should be explored. The inclusion of community development credit unions, for example, would recognize their important contribution to addressing the financial services needs of low-income people which are not met by other financial institutions.

Linked Deposit Programs

Linked deposit programs should explore ways of easing collateral requirements. Where statute and regulation allow for less than 100% collateralization or for flexibility in the types of collateral allowed, this flexibility should be utilized to implement linked deposit programs. Collateral pools and other creative options should be explored to ease collateral requirements without sacrificing the safety of public funds.

Explore the use of pension funds for linked deposits. State and city governments have not tended to utilize pension funds for linked deposits. Linked deposits can be an especially useful type of community development lending for a pension fund because it utilizes a traditional investment vehicle and creates no increased risk to the fund. The use of pension funds would bring several new benefits to linked deposit programs:

1. It would minimize the problems of collateralization, as some types of pension funds can be insured to a maximum of $100,000 per insured beneficiary;

2. It could provide an increased source of funds which is not subject to the same fiscal pressures of general operating funds;

3. It could provide longer-term deposits, thus leveraging a wider variety of linked loans.

Explore expanding linked deposit programs to include community development credit unions as eligible depositories. CDCUs could be a particularly useful vehicle for supporting loans to lower-income households such as mortgages and home improvement loans, or simply to support the basic lending and financial services of CDCUs.

Coordinate linked deposits with other public and private programs with similar goals. One avenue for such a partnership is the program of the Federal Home Loan Bank to provide low interest loans to savings institutions for affordable housing programs. Governments should explore using their linked deposits to increase the impact of those funds and further encourage the participation of institutions in those programs.

Coordinate linked deposit programs with other state or city development agencies and programs. In addition to enabling a more effective program such coordination can bring additional staffing and expertise to usually understaffed finance officers unfamiliar with community development.

General Recommendations

The use of collateral pools to secure public deposits should be further explored. Such pools hold the promise of protecting public funds while reducing the burden on individual institutions. State and city programs without such pools should explore their development.

Further evaluation of the impact of individual reinvestment-oriented public deposit programs is needed. While officials believe that their programs are successful and have a positive impact, the general lack of any objective cost-benefit analysis of a linked deposit program, for example, makes informed decisions about the appropriate expansion of such programs difficult. Evaluation of incentive programs should include assessment of the degree to which additional reinvestment is occurring, financial institutions are competing for deposits through reinvestment programs, or financial institutions are participating in public programs. A more in-depth evaluation of the most successful programs would help encourage other states and cities to develop new reinvestment-oriented deposit programs.

Forums are needed for the sharing of information between cities and states on reinvestment-oriented public deposit programs. Such forums could assist local officials in designing and implementing successful programs and would be especially helpful for discussing the less-well-established incentive deposit programs. Such forums could be created through a conference specifically on public deposits, or perhaps more appropriately through workshops at national and regional meetings of state and city officials.

More aggressive publicity about successful public deposit programs is needed. Public attention to reinvestment

deposit programs gives the program more visibility and greatly adds to financial institutions' incentive to participate. In addition, annual reports of these programs should be published so that the public, community development practioners, legislators, and others can see what has been done.

Reinvestment deposit programs would benefit from greater involvement by appropriate participants from both inside and outside of government. One vehicle for this is an ongoing oversight committee. Such a structure helps ensure that policies are pursued, provides an ongoing constituency for the program, and serves to facilitate partnerships that can create more effective reinvestment initiatives. An oversight committee could include bankers, community developers, farmers, small business and other relevant constituencies, legislators, and development agency staff.

Reinvestment deposit programs can be strengthened by interdisciplinary or interdepartmental input within state and local governments to ensure that those with an appropriate interest and expertise are involved in the program design and implementation. Finance officers should not be left with the sole responsibility for implementing reinvestment deposit programs unless they have adequate staff with development expertise and adequate resources to carry out programs.

Incentive deposit programs and linked deposit programs are seen as complementary efforts to address different reinvestment needs. States and cities should consider an integrated program which incorporates both types of efforts. Such a program would have an overall screening mechanism for all public deposits, a designated fund for special reward deposits, and a program for below market targeted linked deposits. A multifaceted program ensures that even if a local government's fiscal situation precludes linked deposits, it will continue to be able to influence reinvestment in its community(-ies).

In addition to lending criteria for linked and incentive deposits, programs should consider including affordable banking services and lifeline services as the basis for public deposits.

In many cases, it is desirable for public deposit programs to be authorized through legislation. Enabling legislation provides public deposit program administrators the authority and direction to implement programs in situations where they lack the authority to do so administratively. Legislation is most desirable in states or cities in which treasurers or chief finance officers are

not elected and may not have either the authority or interest in implementing reinvestment oriented public deposit programs. In such cases it is helpful for administrators to be given a clear mandate to implement a program, to have goals and responsibilities clearly defined, and to be given adequate resources to implement the program effectively.

In states and cities in which the treasurer or chief finance officer is elected or has a clear policy implementation mandate, enabling legislation may not be required for effective program implementation. In such cases, however, programs may be at risk with changes in administrations.

APPENDIX I

Linked Deposit Program
Profiles - Cities

	AKRON, OH	CONCORD, MA
Date of Origin	unknown	1980
Statutory Authority	No	No
Funds Deposited	$3,500,000	$789,000
% of Allocation	100%	100%
Loan Types	Housing rehab.	Residential construct., mortgages, rehab
Loan Criteria	Conform with City program	Conform with City program guidelines
Terms/Instrument	20 year maximum	Varies
Rates: Deposit, Loan	5% on deposits, 6% on loans, no fees	As low as 0% on deposits
Funding Source	CDBG funds	CDBG funds
Application Procedure	Through City Planning agency, then bank	Through City, refers to bank
Program Staffing	City Planning Dept.	City staff
Marketing	Through City Planning Dept.	By City
Monitoring	City Planning Dept.	By City
Contact Person		Everett Cliff, Diann Writer
Comments/Notes	City guarantees 50% of principal. Places deposit for total loan costs. Bank originates.	

Linked Deposit Program
Profiles - Cities

	KANSAS CITY, KS	KANSAS CITY, MO
Date of Origin	1990	1989
Statutory Authority	Yes	No
Funds Deposited	$1,500,000	$2,350,000
% of Allocation	122%	47%
Loan Types	Rehab of office bldg. to attract major employers	Housing construction, rehab and mortgages, commercial loans
Loan Criteria	Finance rehab project	Low and moderate income census tracts
Terms/Instrument		One year CD renewable up to 4 years
Rates: Deposit, Loan	0% on deposit, 4% on loan	U.S. T. Bill on deposits, market rate on loans
Funding Source	General	Pooled investment funds
Application Procedure	N/A	Through banks
Program Staffing	Treasurer's staff	Treasurer's staff
Marketing	N/A	Through bank
Monitoring	Treasurer's office	City Treasurer checks loan totals
Contact Person	Russell Breitenstein	Janice Reed
Comments/Notes	$250,000 of linked dep. from county, $750,000 from board of public utilities	Deposits must be matched dollar for dollar for designated loan types.

Linked Deposit Program
Profiles - Cities

	LANSING, MI	RALEIGH, NC
Date of Origin	1982	unknown
Statutory Authority	No	No
Funds Deposited	$1,137,000	$125,953
% of Allocation	100%	N/A
Loan Types	Housing rehab	Housing rehab, home mortgages
Loan Criteria	Conform with City redevelopment guidelines	Conform with City development guidelines
Terms/Instrument	unknown	unknown
Rates: Deposit, Loan	50 basis point reduction on deposits, market rate loans with no fees	0% on deposits, flexible reduction on loan rates
Funding Source	CDBG funds	CDBG funds
Application Procedure	Through City Planning and Devel. Agency	Through City
Program Staffing	City Planning and Development Agency	City Devel. Agency
Marketing	City Planning and Development Agency	By City Devel. Agency
Monitoring	By City	By City
Contact Person	Douglas Rubley	
Comments/Notes	Reduced rate deposit to leverage loans with no application or servicing fees.	

Linked Deposit Program
Profiles - Cities

TORRANCE, CA

Date of Origin	unknown
Statutory Authority	No
Funds Deposited	$92,000
% of Allocation	225%
Loan Types	Housing rehab
Loan Criteria	Seniors and low and moderate income housing
Terms/Instrument	unknown
Rates: Deposit, Loan	0% on deposits, 0% on senior loans, 4% on low-mod loans
Funding Source	CDBG funds
Application Procedure	City Planning Agency refers to bank
Program Staffing	City Devel. Agency
Marketing	City Devel. Agency
Monitoring	By City
Contact Person	Alberto Pagdanganan
Comments/Notes	

Linked Deposit Program
Profiles - States

	ILLINOIS	INDIANA
Date of Origin	1967	1985
Statutory Authority	No specific law	No
Funds Deposited	$320,000,000	$72,000,000
% of Allocation	N/A	111%
Loan Types	Agriculture, small business, housing, large commercial	Agriculture
Loan Criteria	General guideline of one job per $25,000 deposit for commercial loans	Growing season loans
Terms/Instrument	1-2 year renewable CD	1-year CD (or less)
Rates: Deposit, Loan	Flexible, generally 250 basis point discount from CD rates	300 basis point discount on CDs, 300 basis point spread
Funding Source	General	General
Application Procedure	Usually bank, borrower apply to state	Through banks and farm credit assns.
Program Staffing	One full-time with some support	2 1/2 full time
Marketing	Brochures, word of mouth	Brochures in banks, public service announcements
Monitoring	Informal	None required
Contact Person	Jack Lavin Roberta Warshaw	Christopher Johnston
Comments/Notes	Program does draw upon some statutes for authorization, but no specific law. Funds used for linked deposits called "specific opportunity program."	1991 cycle in jeopardy due to projected fiscal problems.

Linked Deposit Program
Profiles - States

	IOWA	KANSAS
Date of Origin	1986	1985 (-1989)
Statutory Authority	Yes	No
Funds Deposited	$14,500,000	$15,000,000
% of Allocation		
Loan Types	Horticulture, small business, historic preservation	Small business, agriculture
Loan Criteria		Job creation or retention for small business component
Terms/Instrument		1-year CD
Rates: Deposit, Loan	300 basis point discount from T. Bill rates, 400 basis point spread	300 basis point discount on CD and loan
Funding Source	General	Special Highway fund
Application Procedure	Through banks	Through banks
Program Staffing	One full-time	One full time
Marketing	Brochures in banks, PSA's, talks to groups	Through banks
Monitoring	Review applications, informal thereafter	Reliance on pledge certificates
Contact Person	Lynn Bedford	Lisle Ocobock
Comments/Notes	Seeking funding for impact study of program.	Special fund no longer available. Attempt to pass legislation for use of general funds failed due to lack of

Linked Deposit Program
Profiles - States

	LOUISIANA	MAINE
Date of Origin	1989	Unknown
Statutory Authority	Yes	Yes
Funds Deposited	$150,000	$3,200,000
% of Allocation		80%
Loan Types	Small business, agricultural processing	Agriculture commercial
Loan Criteria	150 or fewer employees create or retain jobs	One job affected per $20,000
Terms/Instrument	1-year CD renewable to 3 years	2-year CD
Rates: Deposit, Loan	300 basis point reduction on deposits, loans	200 basis point reduction on CD and loan
Funding Source	General	
Application Procedure	Through banks to Econ. Dev. agency.	
Program Staffing	None	
Marketing	None	
Monitoring	Penalty for false statements. Informal monitoring	
Contact Person	Yvette Rook Jules Nunn	Maurice Stickney
Comments/Notes	Treasurer places deposit.	

Linked Deposit Program
Profiles - States

	MARYLAND	MICHIGAN
Date of Origin	1989	1987
Statutory Authority	Yes	Yes
Funds Deposited	$1,000,000	$349,000,000
% of Allocation	100%	100%
Loan Types	Small business (fixed assets)	Agriculture
Loan Criteria	High unemployment areas (30% above state average)	Crop loss standards
Terms/Instrument	5-year CD	
Rates: Deposit, Loan	300 basis point discount on CD and loan	0% on deposits, loans; deposits = 120% of loan amount
Funding Source	General: allocated	General: allocated
Application Procedure	Through local govt. agencies	Through banks
Program Staffing		
Marketing	Through local govt. agencies	
Monitoring	State Employment and Ec. Dev. agency reviews unempl. data if deemed necessary. Annual review of loan itself.	
Contact Person	Art Drea	Phillip Wippel
Comments/Notes	Mostly mfg., indus. linked deposits often part of deal with state and local development agencies.	No current activity. Fund expended.

Linked Deposit Program
Profiles - States

	MISSOURI	MONTANA
Date of Origin	1986	1984
Statutory Authority	Yes	No
Funds Deposited	$365,000,000	$1,200,000
% of Allocation		N/A
Loan Types	Agriculture, small business, major industry	Commercial, residential
Loan Criteria	Ten or less employees for small businesses	Job creation credits based on pay level
Terms/Instrument	1-year CD renewable, flexible	Up to 20 years
Rates: Deposit, Loan	300 basis point reduction on CDs, loans	Up to 250 basis pont reduction based on pay level
Funding Source	General	Coal tax trust fund
Application Procedure	Through banks, Ec. Dev. agency, referrals	Through banks
Program Staffing	Six full-time	None
Marketing	PSA's, talks to groups, Econ. Dev. agency referrals	Through banks
Monitoring	Reviewed at application, then informal	Bureau of Labor checks employment data
Contact Person	Richard Hanson	Terry Spalinger
Comments/Notes	State devoting highest proportion of funds to linked deposit program. Also does market rate education loans.	No discount on residential, serves as supply source for fixed rate loans.

Linked Deposit Program
Profiles - States

	OHIO	PENNSYLVANIA
Date of Origin	1983	1988
Statutory Authority	Yes	No
Funds Deposited	$135,000,000	$32,700,000
% of Allocation	12%	16.4%
Loan Types	Agriculture, small business	Small business
Loan Criteria	One job per $25,000 deposited for small bus.	One job affected per $15,000 to $25,000 deposit
Terms/Instrument	1-2 year CD renewable to 4 years	5-year CD
Rates: Deposit, Loan	300 basis point discount for deposits and loans	100 basis point discount on both loan, deposit
Funding Source	General	General
Application Procedure	Through banks	Through banks
Program Staffing	Two full-time	One full-time and 2-4 field examiners
Marketing	Through brochures, PSA's, talks to groups	PSA's, talks to groups, Econ. Dev. agency referrals
Monitoring	Routine review of employment agency data	Annual field exams
Contact Person	Sue Hamilton	Patricia Stoner
Comments/Notes	Pre-program impact study by state legislative budget office.	

Linked Deposit Program
Profiles - States

	TEXAS	WEST VIRGINIA
Date of Origin	1989	1985
Statutory Authority	Yes	Yes
Funds Deposited	$3,800,000	$225,000,000
% of Allocation	76%	
Loan Types	Agricultural diversification	
Loan Criteria	Agricultural crop diversification	
Terms/Instrument		2-year CD
Rates: Deposit, Loan	200 basis point discount from T. Bill rates, 400 basis point spread	300 basis point discount on CDs loans
Funding Source	General	General
Application Procedure	Through banks, processed by Ag. dept.	Through banks
Program Staffing		
Marketing		
Monitoring		
Contact Person		Jerry Simpson
Comments/Notes		Suspended in 1989 due to liquidity problems.

Linked Deposit Program
Profiles - States

WYOMING

Date of Origin	1986
Statutory Authority	Yes
Funds Deposited	$123,000,000
% of Allocation	
Loan Types	Commericial, agriculture
Loan Criteria	Job creation
Terms/Instrument	5-year CD
Rates: Deposit, Loan	300 basis point discount from T. Bond rates 300 basis points off loan
Funding Source	General
Application Procedure	Banks originate, then apply to state
Program Staffing	
Marketing	
Monitoring	
Contact Person	Stan Smith
Comments/Notes	