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INNOVATIONS TRANSFER
New Approaches by the States

INVESTING STATE FUNDS

The Wisconsin Investment Board

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"It is one of the happy incidents of the Federal System that a single courageous state may, if its citizens choose, serve as a laboratory and try novel social and economic experiments without risk to the rest of the country."

Supreme Court Justice Louis D. Brandeis

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FOREWORD

The policy, management, and operations of state government require the application of constantly updated approaches to address changing needs and priorities. This necessity for self-renewal implies innovations in the institutions of state government, in their structure, policies, procedures, and personnel.

Many innovations have occurred in recent years in a number of fields at the state level. However, too little is known about some specific state activities because of the variety of laboratories in which they occur. The innovation process is further complicated by the fact that state government officials rarely have the time or opportunity to share such knowledge which may be applicable in other States. Under day-to-day pressures and constraints, professional administrators and technical experts lack the time to write up or share new approaches that they have developed.

The Council of State Governments, which has been providing a forum for such an exchange for many years, has recently expanded its efforts in this area. The State of Wisconsin Investment Board is one of a series of six innovations being studied by the Council under a grant from the National Science Foundation. Besides this program, the others selected for evaluation during this first year include pension fund consolidation, statewide property tax assessments, a state energy management commission, controlling health costs, and a railroad branch line rehabilitation program. Reports are available on the latter four programs.

The state programs studied were selected by a national advisory panel composed of state legislators and officials. The Council is grateful to these individuals for their assistance: Senator Anthony A. Derezinski, Michigan;sSenator John Pat Fanning, West Virginia; Senator Larry Fasbender, Montana; Representative Vera Katz, Oregon; Walter Kicinski, Deputy Secretary to the Governor, New York; Jeffrey Laurenti, Executive Assistant, New Jersey Senate; Attorney General V. Frank Mendicino, Wyoming; Senator Mike O'Connor, South Dakota; Representative Cornelius O'Leary, Connecticut; Dr. Tibor Payzs, Special Assistant to the Governor, Kentucky; Joseph V. Stewart, Deputy Director, Department of Finance and Administration, Arkansas; Daniel W. Varin, Chief, Statewide Planning Programs, Rhode Island; William W. Wilkins, Budget Director, Ohio.

This report on Wisconsin's Investment Board was prepared by Dick Howard, Director of the Council's Innovations Project, and James E. Jarrett, Research Associate.

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Lexington, Kentucky
August 1976

PREFACE

Inflation, opposition to higher taxes, and taxpayer disenchantment with government generally, are having a serious impact on government financing at all levels. A recent National Association of State Budget Officers' survey showed States' general fund expenditures in fiscal years 1975 and 1976 increased at a faster rate than did general fund revenues. Surpluses built up in previous years have been rapidly depleted. In the aggregate for the 43 States that responded to the budget officers' survey, general fund balances declined from 8 percent of expenditures in 1974 to an estimated 0.3 percent in fiscal year 1976.

The problem is further exacerbated for States by federal funding reductions in some functional areas and federal program requirements for additional state dollars in other areas. All of these factors are beyond control of state government officials.

In a word, state managers should be, and are looking for additional sources of revenue. One obvious source of significant amounts of revenue is to put state dollars to work, and more and more States are taking advantage of investment opportunities. Perhaps no State has a more completely developed investment program than Wisconsin, which has been investing the assets of retirement funds for 65 years.

This monograph is the fifth in the Council of State Governments' current series of reports on innovative state government programs. It probably comes the closest to describing a "model" program. One reason is that the State of Wisconsin Investment Board has had 25 years to evolve.

We are grateful to the many individuals in Wisconsin, especially those associated with the investment board, who were so generous with their time in helping us to understand the agency's activities and responsibilities. In addition to each of the investment directors, we especially want to thank George W. Crownhart, General Counsel for the board and at the time of our visit acting executive director; Gerald T. Mahaffey, Administrator, and Tom Landgraf, Director of State Budget Operations.

Several individuals reviewed earlier drafts and made useful comments: LeRoy Dockter, Audit Director, Wisconsin Legislative Audit Bureau; Peter J. Nelson, Assistant State Treasurer, Wisconsin; George A. Bell, Executive Director, National Association of State Budget Officers; and Carl Vorlander, Executive Director, National Association for State Information Systems.

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August 1976

EXECUTIVE SUMMARY

- The State of Wisconsin Investment Board invests the retirement funds of the major government employee units in Wisconsin: Milwaukee teachers, state employees, and Wisconsin teachers.

- The investment board invests idle cash from 34 different state accounts, earning $56 million on these pooled accounts last year.

- The investment board invests the State's check float, working with the state treasurer and the Department of Administration to ascertain the State's revenue and withdrawals each day.

- The Wisconsin board also has authority to invest the surplus funds of local governments that may deposit such funds with the treasurer.

- The Wisconsin investment program is facilitated by:

  –Use of only one bank for all deposits and withdrawals of state funds. (No state money is deposited or invested in other state banks.)

  –A computerized statewide accounting and reporting system that allows quick and accurate cash flow estimates by the Department of Administration and state treasurer.

  –Use of a custodian bank in New York City that eliminates handling of securities by Wisconsin officials and permits immediate transfers.

  –Great latitude in the types of investment instruments that can be purchased thus permitting the flexibility needed to maximize investment return.

- Almost all aspects of the Wisconsin investment program have been specifically authorized by Wisconsin law.

HOWEVER, other States should consider that *an investment program similar to Wisconsin's*:

- Would reduce the control top elected officials have over the use of surplus state funds;

- Would be opposed by banks which would no longer serve as depositories of public monies, including some local funds in the case of the Wisconsin local government investment pool;

- Would be more difficult to implement if centralized, computerized accounting procedures were not in use;

- Would be almost impossible to implement if the number of bank accounts cannot be kept to a minimum, preferably one or two;

- Would be opposed by agencies which are now managing the assets of retirement funds.

I. INTRODUCTION

The State of Wisconsin Investment Board manages assets of nearly $2.75 billion (6-30-75) which earn about $175 million (based on a reported rate of return of 6.7 percent). Annual gross purchases and sales in fiscal year 1975 approximated $12.75 billion. In addition to the millions of dollars earned from investing the assets of several retirement funds, the Wisconsin Investment Board earns millions of dollars by investing idle cash balances of 34 pooled accounts, including the general fund. In 1975 the average daily balance in the state investment fund was $614 million. The return on these particular investments exceeded $54 million–$28 million for the state general fund and about $26.5 million credited to the other pooled accounts.[1*]

By way of comparison, $28 million is more than the combined amount appropriated from the general fund to the following Wisconsin agencies: Banking ($3.5 million), Insurance ($9.1 million), Regulation and Licensing ($4.9 million), Local Affairs and Development ($5.2 million), and the Executive Offices ($3.4 million).

Not only does state law authorize the investment of almost all state funds, enabling legislation recently authorized the State of Wisconsin Investment Board to invest bank balances upon which the treasurer has written a check, but which from experience the treasurer knows will not actually be paid out by the bank for several days. In other words, Wisconsin invests its "float" in a manner similar to large corporations. In Wisconsin, the check float averages about $3.5 million per day. If the present 7.44 percent rate of return on short-term investments prevails, the check float would return $264,000 to the State–a sum equal to about 45 percent of the investment board's budget.

$576,000 budget for investment board see p. 3

Since March 1976, the State, through the treasurer and investment board, has begun investing idle balances of local governments. Numerous cities are participating in the program. One city reports earnings of $62,000 on a one-month investment of $9.7 million.

There are almost no major governmental retirement funds in Wisconsin whose assets are not managed by the investment board. It also is widely believed that there are almost no idle cash balances of state agencies. The budget of the board was $576,000 in fiscal year 1975 including salaries and benefits of 28 employees, travel, the cost of investment services and outside investment counseling, and various other items associated with housing and supporting the staff. The $576,500 budget means that the direct administrative expenses of managing $2.75 billion in assets was a very low .02 percent. This ratio compares favorably with .2 to .4 percent commonly found in private financial institutions.[2]

The investment program in Wisconsin is facilitated by state laws that require centralized disbursements and centralized receipts. All checks are signed by the state treasurer in one form or another. All agencies must deposit receipts at least weekly and an even shorter time lapse prevails in the case of some large amounts.[3]

Another important facilitator is electronic data processing which is used throughout the accounting and reporting process.

The "state working bank" also plays an important role in the investment program. This bank, selected at about six-year intervals, is the

only depository for state money and it provides a variety of services including lock boxes, telegraphic money transfers, messenger deliveries, credit for after hours deposits, daily reports on the collected cash balances, and other specified services. Use of the working bank precludes the existence of idle cash balances in a number of depositories and permits rapid and accurate accounting of the State's cash position. Thus, all public money is working continuously.

Within its various portfolios, the investment board invests in stocks, corporate bonds, short-term and long-term obligations of the U.S. government and government agencies, repurchase agreements, real estate mortgages, commercial paper, and private placements. Bankers may lobby against reductions or elimination of state and municipal demand deposits and some legislators may occasionally insist that Wisconsin companies should get preferential treatment in the board's investments, but in the final analysis the direct, measurable economic benefits of a sound investment program have prevailed. The income from interest and capital gains has been substantial. Furthermore, the results compare very favorably with similar programs in the private sector, both from the standpoint of rate of return and costs to administer the program.

In the following section, the organization, administrative procedures, legal authority, and investment policies of the board are described. Additionally, there are separate sections devoted to the municipal investment pool and the Wisconsin state working bank.

*Footnotes for this report appear on pages 24-25.

II. INVESTMENT BOARD RESPONSIBILITIES

The statutes assign extremely broad investment responsibilities to the board and also give it responsibility for the selection of the state working bank. Section 25.17 (1) (a) through (zm) enumerate the funds over which the board shall "have exclusive control of the investment and collection of the principal and interest of all monies loaned or invested." The only public money not invested by the investment board is under the control of the Board of Commissioners of Public Lands and the University Board of Regents.

Retirement Funds

The major investment program involves the management of the assets of the State and Municipal Employees' Retirement Fund, the Milwaukee Teachers' Retirement Fund, and the Wisconsin Teachers' Retirement Fund. On January 1, 1975, these three large retirement funds were merged for investment purposes into two categories–a fixed fund and a variable fund. The fund with the fixed retirement benefits has a broad mix of investments that include bonds, stocks, mortgages, and real estate holdings. By contrast, the variable fund is restricted to equities, primarily common stocks. Finally, the board invests the assets of three smaller funds, the State Life Fund, the Insurance Fund, and the Historical Society Trust Fund. Investment of these funds is accounted for separately.

State Investment Fund

Another important investment activity pertains to the State of Wisconsin Investment Board's exclusive jurisdiction over and management of the State Investment Fund. This fund consists of idle cash balances pooled from 34 individual state accounts, such as the general fund, the conservation fund, the state property insurance fund, and the highway fund. Because of the need for flexibility, the emphasis is on short-term investments–repurchase agreements (usually a short-term investment with a bank which is secured by U.S. Treasury bills), reverse repurchase agreements, commercial paper, certificates of deposit, bonds and notes of U.S. government agencies, and U.S. Treasury notes and bills. At one point in November 1975, the State Investment Fund totaled $830 million. The average daily balance invested was $614 million. The high short-term interest rates of FY 1975 permitted returns of 8.89 percent or $54 million.

Local Government Investment Funds

Recently a third investment pool has been authorized and responsibility for its management given to the State of Wisconsin Investment Board. This fund consists of money due local governments through tax sharing, but left with the state treasurer for subsequent board investment–usually short-term. See Section IV of this report for a description of this newest aspect in the innovative Wisconsin investment program.

Investing the Float

In recent years, another important source of investment income to the State has been the short-term investment of "float," that is the difference between the cash on the treasurer's books and the collected cash balance on the working bank's books.

Investing the check float allows checking account balances to earn additional money while outstanding checks are undeposited or are in the process of clearing. Prior to a legislative enactment in 1974, the State of Wisconsin was barred from investing the check float. The attorney general had ruled that all funds disbursed by check had to be payable on demand. Because the State of Wisconsin has an average daily check float of $3.5 million over and above the balance required for services the stakes of investing the excess float are of considerable economic importance. The procedure for investing the float can be illustrated by an example of state employees' payroll checks. If payroll checks are disbursed on Thursday, it is known from past experience that about 4 percent of the checks will clear the state working bank on the next day; an additional 28 percent will clear on Monday; 40 percent will clear on Tuesday, and the remaining checks will trickle in later. Therefore, about 68 percent of all payroll funds can be placed in short-term investments by the investment board for four days (Thursday to Tuesday). The state treasurer's office, after receiving the state working bank's daily report and computing the check float each day, will include these funds in the amount available for short-term investments and transmit this information to the investment board's short-term division.

There is no danger of overdrafts in the normal sense because the State maintains approximately $10 million as compensating balance at the working bank. If the compensating balance goes below the minimum requirement, a charge is carried forward the next month against the State's account.

Revenues generated by investing a State's check float will vary depending on the average daily float and short-term interest rates. In Wisconsin, with an average daily float of $3.5 million, the annual income generated would be as follows based on various short-term interest rates (income computed on 360-day basis):[4]

5 percent	$177,000
6 percent	$212,000
7 percent	$245,000
8 percent	$283,000
9 percent	$319,000
10 percent	$354,000

The most recent return on the State Investment Fund was 7.44 percent which, if maintained for the remainder of 1976, would bring the State nearly $264,000 this year. As one Wisconsin official noted, "With respect to the over $3 million per day typically tied up in check float, the situation is simple: either the bank makes money on it or the State of Wisconsin does."[5]

State Working Bank

One other important, but noninvestment-related, function assigned by the Legislature to the board is the designation of the state working bank. This bank is the depository for all of the State's funds. With few exceptions, it provides the State with all its banking services. See Section V of this report for a description of the state working bank.

Development of the Wisconsin Investment Program

The 28-person staff, the five investment divisions, and the several investment pools managed by the investment board are the present characteristics of an ongoing investment process that can be traced to 1911 and the creation of the State Annuity Board. Actually the board superseded the Annuity and Investment Board which by 1947 already exercised centralized control of investments, having responsibility for both idle operating funds and retirement trust funds.

At the outset, the Board of Trustees consisted of seven persons including the Governor, who was chairman. The staff numbered three. The investment board had the authority, even then, to invest in real estate, mortages, common stocks, preferred stocks, and U.S. government securities.

Over the years, many changes have brought additional retirement and operating funds under the jurisdiction of the investment board, streamlined the administrative procedures, expanded the types of investment instruments available to the investment board and reduced the day-to-day role of the trustees vis-a-vis the staff. As the changes occurred and the assets under management increased, the size of the staff also increased although less rapidly.

In 1957 the State Investment Fund was created by the Legislature when it consolidated 19 different operating and temporary reserve funds into one. The Legislature also created the fixed annuity and variable annuity funds for each of the retirement trusts as a response to inflation.

By 1958, the third of the major retirement funds, the Milwaukee Teachers, placed its assets under the board's control.

The actual physical storage and handling of securities by the state treasurer's office ended in 1970 when the Legislature authorized the board to maintain an account at a non-Wisconsin bank. In that year, a custodian account was opened at a New York City bank for equities and a couple of years later an account for bonds was established at the same bank.

In the past three years, the trustees have prepared a policy manual delegating considerable authority to the staff;[6] the State has begun investing its cash float; the local government investment fund also has come into being; investment in longer term U.S. government obligations and unsecured notes of corporations including certificates of deposit has been authorized along with reverse repurchase agreements in a general effort to allow greater earning power and flexibility in short-term investments. The three major retirement funds have been merged for investment purposes greatly reducing the accounting work and enabling the fixed portfolio to be improved by amortizing gains and losses over a period of slightly more than 14 years (see page 00).

The Politics of Investing State Funds

The investment board is apolitical and most observers agree that political pressures are minimal. However, with this much money, there are always interest groups endeavoring to have the funds benefit them or their causes. Two groups have, in fact, "borrowed" a substantial portion of the General Fund portion of the state investment pool: (1) the board must make available at the request of the Department of Veterans Affairs up to $16.5 million for the purpose of housing loans to veterans, and (2) upon the request of the higher educational aids board a cumulative total of not more than $55 million for loans to needy students.[7]

Not surprisingly, some underlying pressure is reflected in some legislators' views—to increase the percentage of brokerage business done with Wisconsin brokers and to give preferential treatment to Wisconsin companies when making loans and investments. In addition to the pressures for geographic preferences, there are from time to time pressures to give preferential treatment to minority businesses, and to avoid investments in companies engaged in "socially undesirable activities."

Social goals not pursued as a part of investment policy

The independent nature of the board reinforces the individual member's inclination in the role as trustee not to pursue social goals in investment policies, and the Legislature has not mandated that social goals should be an investment consideration. Another factor mitigating against social issue criteria is the inability to agree upon and measure social benefits versus the clearly measurable results of economic decisions. An 8.26 percent return is an 8.26 percent return and it is better than a 7.26 percent return.

Although investment directors do not in fact give weight to social criteria the Board of Trustees cannot and does not take a "public be damned" attitude. It is aware that it operates in a political environment.[8]

III. ORGANIZATION OF THE INVESTMENT BOARD

The State of Wisconsin Investment Board consists of seven members, six of whom are appointed by the Governor to staggered six-year terms. The seventh trustee is the secretary of the Department of Administration or the secretary's designee. Four "public" members must have at least 10 years of experience in financial matters (Wisconsin Statutes 15.79[2]), and the other gubernatorial appointees are nominated by the Wisconsin Teachers' Retirement and the State Employees Retirement Fund, respectively. The trustees generally meet for two days a month.

Staffing

Actual investments–purchases and sales–are made by the staff acting under general policy guidelines set out by the seven-member Board of Trustees.[9] The staff is headed by an executive director who serves at the pleasure of the trustees. The staff presently numbers 28, and one more position has been authorized for the 1976-77 fiscal year.

Reporting to the executive director are five investment directors, each of whom is responsible for a three- or four-person division. The investment directors are appointed by the executive director with participation of the trustees. The investment director positions are part of the Wisconsin State Civil Service System and incumbents, after a probationary period, can only be terminated for cause. (Poor performance can be cause and investment directors have been terminated on that basis.) In addition to the investment directors, there is an administrative officer who is in charge of office operations such as personnel, accounting, secretarial, and clerical services.

The structure of the organization is in the process of changing. A research division is being created which will consist of a research director and four analysts. Previously, there were two research analysts and they reported to the investment director for stocks. Under the new arrangement, they will continue to analyze industry groups, but as the change suggests, will provide support services to all five investment directors.

Despite the existence of these research specialists, the board primarily relies on New York and selected regional investment banking firms for firsthand research of particular companies.

Salary ranges for top positions are shown below. While it is generally agreed that salaries for comparable positions in the private sector are higher, the investment board is able to fill its positions with competent individuals.

Position	*Salary Range*
Executive Director	$31,068 - $43,500
Investment Directors	$28,512 - $39,912
Research Director	$17,016 - $23,820
Senior Research Analyst	$14,316 - $20,040
Junior Research Analyst	$10,368 - $13,896

The day-to-day investment decisions are made by the investment directors with the concurrence of the executive director.[10] Quarterly, the investment directors and the executive director meet to determine how the estimated revenues will be allocated among the divisions: stocks, private placements, corporate bonds, short-term, and mortgages and real estate. Allocation depends on their collective judgment of market and investment opportunities in forthcoming months. Their views are also considered by the Board of Trustees, who retain the services of outside financial advisors.

Some funds such as those earmarked for the variable long-term investment fund, for example, all go to the investment director for common stocks. He decides on the timing and brokers for his purchases and sales, as do other investment directors for the funds allocated to them during the quarter.

Long-term investments for the fixed fund are generally invested by the Bonds, Private Placements, and Mortgages divisions. The short-term investment division is responsible for investing the 34-fund pooled account, the "float" funds, and the new local government investment funds.

Table 1 shows the diversified types of investments managed by the State of Wisconsin Investment Board.

Table 1

State of Wisconsin Investment Board
Assets Under Management
(June 30, 1975)

Public Bonds	$829,000,000
Bonds, Private Placements	322,000,000
Stocks	876,594,000
Mortgages	174,513,000
Real Estate	26,283,000
Short-Term	488,190,000
U.S. Treasury Notes & Bills	40,100,000
Government Agencies	86,670,000
Commercial Paper	105,945,000
Repurchase Agreements	255,475,000

Source: State of Wisconsin Investment Board, *Annual Report* Year Ending 6-30-75

Investment Division—Bonds

Bonds are a major part of the fixed fund portion of the long-term investment portfolio. During FY 1975, the Wisconsin board invested $90.7 million in publicly issued bonds and $45.2 million in private issues. All bonds account for approximately one-half of the long-term assets managed by the board, $1,150,955,949 or 51.8 percent on June 30, 1975. The public bonds portion was $829 million. Interest income on public bonds was $36 million for the fiscal year.

Investment in corporate and government bonds is not unique to Wisconsin. In Wisconsin, specific authority to invest the fixed retirement investment trust, the state life fund, and the veterans trust fund is contained in Section 25.17 (3) (a) of the Wisconsin code. Statutory limitations on such investments are spelled out in Section 206.34 of the

Wisconsin statutes of 1969. Regarding the bonds of industrial corporations the investment board may not invest more than 2 percent of its assets in any one company nor may it invest in a company that has defaulted in the payment of principal or interest on its indebtedness within the past five years.

In addition, under the policies established by the Board of Trustees, all bonds purchased must be rated by two approved rating organizations. With regard to AAA bonds, no more than 2 percent of the fixed funds assets may be invested in any one issue; for AA or A the limitation is 1 percent and for Bbb or Baa, up to .25 percent. Baa and lower rated credits are reviewed annually.

Excluding portfolio improvement transactions (discussed below) an average of two issues of bonds is purchased each month. There is no policy that places emphasis on the credit issues of Wisconsin companies. However, it is the practice of the Bonds Investment Director to try to give Wisconsin bond dealers 50 percent of the "new issues" business where possible. To give Wisconsin dealers most of the bond business would preclude the division from receiving the research of New York based brokerage firms. The bond portfolio is now computerized by a brokerage house and each month a printout of the bond portfolio is sent to the investment board.

Transaction Amortization Account

The 1975 merger for investment purposes of the three major retirement funds facilitated another important change in investment procedures, particularly in the purchase and sale of bonds and stocks. It enabled the board to create a "transaction amortization account" whereby profits or losses from the sale of assets are spread over a 14-year period. Traditionally, most agencies investing public funds have applied profits or losses resulting from the sale of assets to the earnings of the year in which the sale occurred. One result was a certain inflexibility in portfolios since most portfolio managers were reluctant to sell assets resulting in large "book" losses that would be charged to the current year's investment income.

By merging the three retirement fund investments, it was no longer necessary to maintain records on each series of assets held in the portfolio. All gains or losses could be debited or credited to one account. The next step was to amortize all profits and losses at the rate of 7 percent annually, or slightly more than 14 years for the fixed retirement fund.

Among advantages reported are: (1) savings in work load, time and dollar costs by no longer amortizing each security, (2) a smoother, more representative and equitable annual income, and (3) greater flexibility in bond portfolio management. In fact, the Wisconsin board reports that in the first six months after the new accounting procedures were instituted, 24 separate "portfolio improvement transactions" changed the average annual yield on these investments from 7.633 percent to 9.007 percent. The book loss was $4 million, $33.4 million par value sold and reinvested in bonds having a $29.4 million par value.[11]

Investment Division–Stocks

Common stocks comprise almost 100 percent of the "variable fund" and a substantial part of the "fixed fund." In FY 1975, for example, 28 percent of the board's fixed fund cash was invested in common stocks. During the fiscal year, common stock purchases totaled $152 million, and total sales were $102 million.[12] As of June 30, 1975, stocks accounted for 39.5 percent of the State of Wisconsin Investment Board's long-term assets (variable and fixed funds) and were

valued at $376.6 million. In the fiscal year, the market value of the stocks in the fixed fund rose 20.8 percent and variable fund, 25.3 percent compared with a 16.1 percent of the S&P 500 Index—the most commonly used measure for evaluating performance of the Stock Division.

Stock transactions are made daily and net purchases average roughly $30 million a month. Commissions approximate $1 million annually in return for which the Wisconsin Investment Board receives considerable research.

Wisconsin's law [Chapter 25.17 (3) (a)] specifically provides that funds in the fixed category from the three major retirement programs may be invested in accordance with 1969 statutory provisions [Chapter 206.34]. The statute states that purchases of stocks can only be made from companies whose earnings meet certain specified criteria; no more than 1 percent of the investing agency's assets may be invested in the common stock of one company; nor may the equity position exceed 15 percent of the company's assets.

The Board of Trustees has delegated to the staff (Investment Director—Stocks) authority to purchase or sell stocks. However, stock purchases must be from the trustee-approved list of 206 companies. The investment director must also adhere to the trustees' policy limiting stock portfolio assets in any single industry to 15 percent, and no more than 30 percent may be invested in any one of the following broad categories: basic industry, consumer, technology, government regulated, and financial.[13]

The investment director reports that these constraints cause no particular problems and that the stock portfolio includes ownership in 120 companies.[14] A major criterion of the investment director is that an $8 to $10 million equity position will be possible in any company whose stock they might purchase. Because these stock investments usually do not go directly to companies, there is no pressure to buy the stocks of Wisconsin companies.

Investment Division—Private Placements

Might be instructive to explore the reasons why Wisconsin places a majority of its loans outside the state — What are the policy considerations - - -

Presently, $400 million (all from the retirement funds) is invested in private placements. According to the director of the division, "the major reason for inclusion of private placements in the portfolio is to realize an above average return on investments, through assumption of somewhat above average risk plus a premium for lack of marketability."[15]

The division currently has outstanding loans to 300 companies across a variety of industries: railroad, oil, savings and loan, foundry, retail chain, utility, and various manufacturing companies.[16] Loans are not restricted to Wisconsin; the majority of private placements are in other States and Canada.

Is this statutory? Should there be "stated ratios?

Criteria for a private placement investment are rather strict. The two most important ratios analyzed are that long-term debt will not exceed 40 percent of total capitalization and that the sum of pretax earnings and fixed charges will be three times the fixed charges for the last two years (a 3 x fixed charge coverage ratio). The minimum loan is $2 million and no credit rating of less than Baa will be considered. Placements cannot be used as venture capital—no loans can be made to companies in existence for less than five years.[17]

If the application has met this initial set of criteria, placement division staff request additional financial material and check many standard accounting measures such as rate of return on sales, operating margins, tax rates, and cash flow position. Also, the staff will consult

with outside people and solicit opinions on the company and industry, and may make site visits to the company.

There have been instances of legislators criticizing the private placements division for not loaning more money to Wisconsin firms. Concessions in the quality of the company or in the quality of the loan have not been made for placements in Wisconsin, but there are some allowances made for Wisconsin placements in terms of company size and requested loan figures. For companies outside the State, the minimum loan is $2 million, and only those whose annual sales are at least $40 million are considered. Wisconsin-based companies may request a loan as small as $1 million provided their annual sales are at least $15 million. Recent loan yields have averaged nearly 10 percent and it is estimated that fewer than 10 of the 400 loans outstanding are problems.

Investment Division–Mortgages and Real Estate

At present it is the board's policy that mortgages and real estate investments shall comprise between 5 and 25 percent of the fixed-fund portfolio. On June 30, 1975, nearly $200 million was invested in mortgages and owned real estate. Return on mortgage and real estate investments exceed that of the bond division. The average return on the mortgages division's portfolio was 7.34 percent as of June 30, 1975.

A detailed set of guidelines is used by the three staff members of the division in determining which mortgages and real estate opportunities will be funded.[18] As with the other divisions, all investments of the mortgages division must conform to the broad specifications for investments set forth in the 1969 statutes.[19]

There is a broad diversity of mortgage fundings. In 1975, over $51 million was loaned to 16 income properties–two shopping centers, eight apartments, two warehouses, a medical clinic, a nursing home, a manufacturing facility, and a participation in a loan on an office building. While there is an emphasis on mortgages and real estate investments in Wisconsin, more than 75 percent of the division's portfolio is placed outside the State.

Investment Division–Short-Term Investments

The short-term division has responsibility for investing the state investment fund which consists of 34 separate accounts such as the general fund (including the check float), highway fund, local government pooled investment fund, and cash of the retirement systems prior to its long-term commitment. Assets managed by the two members of the division vary from $600 million to $1 billion. As of May 15, approximately $775 million was invested by the division. Daily purchases and sales average approximately $75 million, and the short-term portfolio turns over every few weeks.

Return on the state investment fund was 9.02 percent in fiscal year 1974, 8.89 percent in fiscal year 1975, and 7.44 percent in the most recent quarter ending March 31.[20] The 7.44 percent rate of return for the recent period, as other state officials will note, is an excellent return since it was 1-1/2 to 3 percent greater than interest rates generally available to large cities. Declining short-term rates in the last 18 months are attributable to national trends.

A variety of short-term investment devices are used: government agency paper, bank certificates of deposit, open day-to-day and term-repurchase agreements, commercial paper, and reverse repurchase agreements.[21] In mid-May, the assets were distributed as follows: government paper – $590 million ($85 million was invested in a single U.S. treasury bill); certificates of deposit – $55 million; open end repur-

chase agreements – $60 million; and commercial paper – $70 million. Usually no investments under $1 million are considered, or agreements under $5 million made.

Operationally, the short-term division receives a computer printout every day before 7:30 a.m. listing all current investments and specifying the present value for each discounted security. By 11 a.m. the division will have been notified of the check float level, will have balanced off the State's cash position, and will have checked over vouchers and amounts for individual transactions. After 11 a.m., the division will make trades for the following day, including making sales to cover the State's disbursement needs for the following day.

Investments are selected by the short-term staff from information supplied by brokerage houses and from staff's own knowledge of the short-term markets. The board's in-house research staff is not utilized regularly because forecasting is less useful for short-term investments than for long-term bonds and stocks.

In the future, the short-term division, in hope of increasing its options and of obtaining an even greater return on the investment fund, will request authority to invest in bankers' acceptances and "Eurodollar" certificates of deposit (the debt securities, in U.S. dollars, of overseas branches of U.S. banks). The ability to sell short in the market also is a possible future investment avenue of the division although the board's trustees have not yet given their consent for this more sophisticated and greater risk investment activity.

Administrative Expenses

An important feature of the investment board's operations is its low administrative expense. Table 2 compares the board's assets to expense ratio with those of private insurance companies and nonprofit investment operations. The Wisconsin Investment Board's expenses are proportionately lower, and in all but two cases (College Retirement Equities Fund and the Illinois Investment Board) the board's expense ratio is one-fifth that of other organizations.

Table 2

Ratios of Assets to Expenses, Selected Comparisons, 1973

ORGANIZATION	*INVESTMENT ASSETS*	*INVESTMENT EXPENSES (EXCL. TAXES)*	*PERCENT*
Acacia Mutual Life	$ 607,881,098	$ 2,774,004	0.456%
Allstate Life Insurance	357,674,020	415,023	0.116%
Aid Assoc. for Lutherans	1,086,948,891	1,479,078	0.136%
Connecticut Mutual Life	3,116,740,666	57,082,944	1.831%
Continental Assurance	1,818,404,188	4,138,855	0.227%
Equitable Life Ins.	14,971,951,691	57,530,742	0.384%
Franklin Life Ins. Co.	1,433,098,891	2,754,778	0.192%
John Hancock Mutual	10,391,836,359	29,414,166	0.283%
Lincoln Nat'l. Life	2,410,340,286	3,649,828	0.151%
Mass. Mutual Life	4,795,468,874	17,907,492	0.373%
Metropolitan Life Ins.	30,286,075,837	99,071,174	0.327%
Mutual Life of N.Y.	4,044,504,230	16,058,497	0.397%
College Retirement Equities Fund	$ 2,600,056,231	$ 1,611,552	0.062%
Teachers Ins. & Annuity Assoc.	3,370,887,045	4,657,944	0.138%
Illinois Investment Board	793,726,994	643,628	0.081%
1974 Investment Board	2,520,303,000	524,468	0.0208%

Source: Wisconsin Investment Board

The investment board's administrative expenses are two cents per $100 of invested assets. As Table 2 shows, in 1974 administrative expenses stood at .0208 percent of assets. This represents a slight decline over the past decade, during which time assets have tripled while staff has doubled. In 1965, the percentage for administrative expenses was .0289.

Several factors may account for the board's low administrative expenses. First, the number of staff and their salaries are less than comparable to private financial institutions. Second, because most funds managed by the board may be pooled, there are significant benefits achieved by a concentration of capital in terms of broker and trader commissions. Third, the board, by being a large institutional investment operation, receives research and related services as a result of its commission fees, that is, no cash outlay. Fourth, the board, like most state agencies, minimizes expenses for amenities and other perquisites.[22]

IV. STATE-LOCAL FISCAL COOPERATION

In February 1976, a bill was enacted in Wisconsin which may produce significant economic benefits for local governments in Wisconsin as well as Wisconsin state government. Senate Bill 788 (reprinted in Appendix A) created two local government investment funds to be managed by the investment board—the pooled investment fund and the trust investment fund. The pooled investment fund is already in operation and will receive the bulk of attention in this section.

The pooled investment fund is a voluntary mechanism by which counties, cities, villages, and towns can deposit with the treasurer any state-shared taxes, local revenues, or idle reserves for investment by the state investment board. The interest earned, equivalent to the rate of return for all short-term investments by the board, is credited to the local government, and funds can be withdrawn on one-day notice with no penalties. The trust investment fund permits local governments to establish their own investment accounts with the state investment board and to have their funds managed for a specific period of time.

Background

Legislation authorizing the pooled investment fund was first introduced by the state treasurer in 1967 but was withdrawn after 11 days because of pressure from the banking community. Because of a temporary (15-day) cash flow problem in Wisconsin state government, the program was revived with modifications in the spring of 1976. The State, which needed cash to disburse real property tax credit payments to local governments, was and is prohibited from borrowing more than $100,000 for current obligations and is prohibited from interfund transfers. Therefore, local municipalities were faced with receiving a prorated amount of their shared taxes. State officials, however, knowing that Wisconsin municipalities collected their main revenues – property taxes – prior to February 28, reasoned that the temporary cash flow crisis could be averted if enough municipalities would defer receiving their state payment for two weeks. As an inducement for such "loans," local governments would receive interest equivalent to that received on short-term investments of the investment board. Nineteen local governments left their funds with the State, and the temporary cash flow crisis was solved.

The pooled investment fund passed the Legislature under propitious circumstances. There was a fiscal crisis situation and the State's bankers were unorganized. While conditions in other States may not be similar, the economic benefits produced by establishment of a pooled investment fund might be sufficiently compelling to overcome opposition.[23] A major hurdle in Wisconsin was obtaining the support of local officials who were concerned about allowing the State to retain their funds in the pool. The local treasurers' association went on record opposing the investment pool. Opposition to the pooled investment trust was softened, however, by also providing for an investment trust fund which would require individual accounts for each locality's funds and for a specified time. If used, the trust fund will not offset the State's cash flow problem since these funds will be tied up for specified periods of time and thus be unavailable to the State.

Provisions of the Two Local Funds

Senate Bill 788 specifies the major similarities and differences between the pooled investment fund and trust investment fund. First, for both funds, local government officials would tell the state treasurer whether they prefer to have their portion of shared taxes paid directly to them or deposited in their account in one of the funds. Secondly, both funds permit local government officials to augment their accounts in the investment board with idle reserves and any other local funds available for investment. Third, for both funds, a maximum of one-fourth of 1 percent of *earned income* will be deducted by the state investment board for administrative costs.

Fourth, local money in the pooled investment fund, while credited to individual local government accounts, would be pooled with state funds for short-term investments. Local money in the pooled investment fund would earn interest based upon the average yield of all short-term investments determined quarterly by the investment board. Local funds in the trust investment fund would not be commingled with other local funds or state funds and unlike the pooled fund, interest on trust investments will be determined by the yield on each separate local government account.

Fifth, local officials depositing funds in the pooled investment fund need not specify on what date they would like their principal and interest returned. Local officials depositing funds in the trust fund must designate the length of investment time for their funds, and incur any financial penalties for early withdrawal of their monies from the trust fund.

How the Pooled Investment Fund Works

The mechanism for direct transfer of local government funds from the state treasury to the investment board serves two functions: (1) it reduces the amount of time which local government funds would sit idle and not receive interest, and (2) it helps the State handle emergency cash flow problems.

Operationally, the deposit and withdrawal system is quite simple. If a local unit of government is depositing money in the pooled investment fund from its state shared taxes, that government gives the state treasurer written instructions as to the amount which the State should retain. If a local unit of government is depositing idle cash from its own treasury, the local treasurer would ask the local government's commercial bank to transfer the funds to the state treasurer for deposit in the investment pool. The investment board will receive its information from the treasurer's office and it will be included in the daily total cash figure which can be invested. The investment board is not notified by the towns directly.

For withdrawals, the same process would be used. If notice of a partial or total withdrawal of the municipality's funds is made by 10 a.m., the state treasurer's office will issue a check that same day and transfer by telegraph the funds to the working bank of the local government. If the check cannot be issued until the next day, the local government also would be credited with an additional day's interest.

The interest earnings are computed on an average yield for a quarter and are based on the average daily balances of each participant's share of the short-term investment fund. Computer programs are used to determine the balance, deposits and withdrawals on a daily basis for each local government.

Advantages of the Pooled Investment Fund

Both the local governments and the State should benefit from this investment pool. For the State of Wisconsin, the new arrangement of localities voluntarily leaving their funds will provide a mechanism to help it deal with the periodic, temporary cash flow problems. In turn, the State's credit rating will not suffer because of frequent cash flow difficulties. Local government funds provide additional capital to the state investment fund; therefore, the state agency may experience a better rate of return on investments and realize economies of scale on the cost side. Moreover, any constant flow of new short-term capital from local governments will enable placements in those investments that are providing the best current rate of return—thus possibly raising the overall rate of return on the State's short-term investments.

Increased cooperation between state and local fiscal officials, it is hoped, will reduce the distrust of state government by local government officials. Finally, to the extent localities experience an improved financial status, the State benefits indirectly.

For local units of government, the pooled investment fund will operate as a checking or demand account which pays a higher rate of return than local governments could obtain on their invested funds.

Officials in the Wisconsin Department of Administration conducted a comprehensive analysis of local government investment practices and discovered that 81 cities and 67 percent of all towns and villages in Wisconsin received no interest income in the 1974 calendar year. Many local officials simply placed idle cash reserves in noninterest bearing demand accounts in local banks.

Local governments should get higher returns on their funds because the investment board can invest in high-yielding, short-term investments such as repurchase agreements and commercial paper, because of lower dealer fees and because of the greater expertise of the board's professional staff. For example, because local governments will receive the same rate of return regardless of whether they invest $2,000 or $200,000 (that is, there is dollar averaging across investors), smaller towns and villages most likely will receive higher interest than if their accounts were invested separately.

In addition, the pooled investment fund, by providing local officials an alternative investment option, may force banks to provide more services to local governments in order to maintain the locality' operating funds.

For some municipalities the flexibility of the pooled investment fund will permit an integration of local governments' investment policies with their cash flow system. As noted previously, local governments may invest funds for any amount of time—one or two days or much longer periods. This "variable date" provision ensures that municipalities will not be penalized for early withdrawal or caught in a cash flow problem because of illiquid investments. In fact, the liquidity of the short-term investments and the mechanism for rapid transfer of funds from the state treasurer to local treasurer will enable local governments to receive their funds on the same day or one day after their notice of withdrawal.

Costs involved to state and local governments from the local government pooled investment fund are nominal. Local governments, in fact, incur only the costs of a phone call or postage for a letter to the state treasurer. The state investment board, as stated in the legislation, will deduct a maximum of one-fourth of 1 percent of all earned interest for administrative expenses. It is anticipated the actual administrative costs will be significantly less than this amount.

One possible difficulty that could arise for the State involves money left by local governments in the general fund at the request of state officials, for use in temporary cash flow difficulties, which is not invested but distributed to local governments who need their share. Lender local governments will receive interest on these funds just as if they were being invested by the investment board. Since these funds were not invested, there is an interest expense for the State that must later be appropriated from the general fund. It is not clear how much of a problem this will be and state officials do not agree. While there is a cost to the State of Wisconsin associated with operating the pooled investment fund during cash flow difficulties, this cost will be less than through borrowing on the short-term markets which is not legal under present law. Of course, any final solution to the cash flow problem must await statutory changes that spread payments throughout the year rather than require very large payments once or twice a year.

The Investment Trust Fund

As established, the local government trust-investment fund will be a vehicle for longer-term fixed investments by local governments. The trust fund, then, is conceived as a different type of investment option than the pooled investment fund.

Unlike the pooled investment fund, capital in the trust fund cannot be used by the State for cash flow purposes because it is in fixed investments. In terms of administrative/bookkeeping costs, the trust fund also is less advantageous–the Department of Administration must set up an individual account for each municipality (potentially 1,400) and maintain records on the type of investment interest earned, compute penalty charges for early withdrawals, and set up procedures for notifying local governments when their investments have become mature. In contrast, for the pooled investment fund, the Department of Administration, in cooperation with the state treasurer's office, needs only to maintain records on the average daily balance of a municipality's account during each calendar quarter as all accounts will receive the same rate of return.

If most local governments use the trust fund for long-term investments (over six months), the administrative task would be manageable, although still an additional burden to the investment board. If local governments wish their funds to be managed and rolled over frequently in short-term investments, the board might be overwhelmed, given present staffing.[24]

Initial Results of the Pooled Investment Fund

The pooled investment fund became effective March 1, 1976, with $61.5 million in deposits from local governments that left their state shared taxes with the State to assist with cash flow problems. After the temporary cash emergency, local governments withdrew over $45 million. Five cities kept their shared taxes in the investment pool during the month of March and received a 7.44 percent rate of return, the overall short-term investment yield for the first three months of 1976. Madison, Wisconsin, earned approximately $62,000 on its one-month investment of $9.7 million.

Overall, the pooled investment fund has been well received, and now, after the initial period of communicating the details of the program to local officials, participation is increasing. In one two-week period in mid-May, 26 additional local units of government invested cash in the pooled fund. As of July 12, 1976, local governments had nearly $28 million in the fund.[25]

Start-up costs of the pooled fund were minimal as coordination for the program involved no budget and limited staff time. It appears no additional state employee must be hired for investment purposes. One person may be hired to serve as the principal information and resource contact for local governments although a final decision has not been reached.

Few complaints have surfaced to date. One city treasurer who has left shared taxes in the pool and also has transferred an additional $2.1 million of the city's cash to the pool sees only two needed modifications. First, according to this official, the investment board should disseminate brief biweekly or monthly reports on what types of short-term investments are being made. This information, he suggests, would be useful for his own investment operation and could also be used to inform the elected city officials that the pooled fund will provide a superior economic return.[26]

Secondly, the city treasurer hopes that when local governments withdraw their funds from the pool, the interest will be returned immediately with the original funds. Currently, earned interest will be returned at the end of the next calendar quarter when the investment board computes the rate of return on short-term investments. Local treasurers can, of course, make estimates of their cities' interest income.

Implementing the Pooled Investment Fund in Other States

In Wisconsin, the pooled investment fund benefits state and local treasuries. In States without a centralized investment unit, establishing an investment mechanism for local governments would be considerably more difficult. States without financial expertise in short-term investments probably should not initiate a pooled fund until an investment board is operational for several years or until appropriate staff can be hired. States with an existing investment agency will need to consider how a sudden influx of local funds will alter current operations. For instance, computer programs must be developed by the investment agency or treasurer's office for proper crediting of municipal accounts. And, until other States duplicate Wisconsin's rapid deposit and withdrawal system, some mechanism must be established so that local governments do not lose substantial interest income from slow transfer of funds.

Not all States may wish to assume additional functions and not all States would receive as many economic benefits as Wisconsin. If a State is not investing in the short-term area, local government funds would not permit a concentration of capital and higher yields. If a State is not experiencing cash flow problems or distributing large sums of cash to local governments, the pooled fund would be less attractive. If there are many cities with their own investment programs, participation in the pooled fund would be less beneficial.

The pooled investment fund would appear to offer many economic benefits to state and local governments, given an appropriate investment framework. This fund will not solve any major existing problem but it may generate state and local revenues without extracting these resources from reluctant taxpayers. Few programs can be assessed so favorably.

V. THE STATE WORKING BANK

Another aspect of the overall cash management system in Wisconsin is the "state working bank." The state working bank is selected by the State of Wisconsin Investment Board. Authority for selecting the bank is found in Section 25.17 of the Wisconsin Statutes:

> (61) [The Board Shall]. . .designate public depositories for the deposit of public moneys. . .coming into the hands of the state treasurer; allocate the deposits of all public moneys coming into the hands of the state treasurer, and limit the amount of such public moneys, as determined from the state treasurer's records, which may be deposited in any public depository so designated. . . .only such banks as have been named by the investment board as working banks shall carry state deposits on which checks are drawn to conduct the daily business of the state, all of which deposits shall be payable on demand.

The Legislature wisely avoided enumerating the selection criteria leaving that task to the board. Although the law would permit more than one working bank, the State of Wisconsin Investment Board has concluded that the operational advantages of using only one bank outweigh any operational or political disadvantages. Thus, there is only one Wisconsin bank serving as a depository for the State's funds. There are both operational and fiscal advantages from having one state bank instead of two. Coordination among a single working bank, the investment board, and the treasurer's office is an easier task because of a single disbursement account. Fewer man-hours are required to resolve any problems or issues when there is only one bank and better service usually results from having a super account with one bank instead of medium-sized accounts with two banks. The use of one bank instead of two has a fiscal benefit as well in that no interest will be lost due to transfer time between banks.[27]

The state working bank in Wisconsin is selected on the basis of proposals submitted by the interested banks.[28] Under the most recently used procedures, there is no ending date—a six-year working arrangement has been normal. It is anticipated that a thorough review of costs and services will occur at two-year intervals. Either the State or bank can terminate the arrangement with 12 months notice.

Activities of the State Working Bank

As banker for the State, the First Wisconsin National Bank will provide many of the services it provides for its largest corporate customers. In its relations with its banker, the State's objectives are the same as a corporation's: (1) accurate reflection of its cash situation at any point in time, (2) efficiency in the provision of services at a reasonable cost, and (3) rapid and accurate transfer of funds in order that the State can make maximum earnings on its funds.

The state account ranges from $2 million to $100 million on any particular day. Thus, the volume of work is considerable. During the year, there will be eight million deposit items to the state account that must be processed. There will be 4.6 million checks and 4.5 million

reconciliation items directly related to the state account.[29] Deposits are made by mail, lock box, wire transfer, and over the counter. All disbursements are made by check with several series currently being used.[30]

Although there may be numerous modifications and refinements in the procedures followed by the State and the working bank, the essential services required by the State are reasonably well defined by the investment board, state treasurer, and Department of Administration. Based on these services and the anticipated volume, the bank's bid for the State's account. Among the services needed are:[31]

(1) The minimum time of credit shall be at least that provided by the Milwaukee Office of the Federal Reserve Bank of Chicago

(2) The state working bank, if located outside Madison, shall designate a Madison bank to serve as its agent and accept all deposits made on behalf of the state treasurer,

(3) Special courier runs from the state treasurer's office to the Federal Reserve Bank and to Chicago Loop banks to collect large dollar items,

(4) Lock box services used by employers for withheld state income taxes and also for motor and special fuel taxes,

(5) Same-day transfer of funds for settlements resulting from short-term investments,

(6) Normal checking services plus separate reconciliation for each of several series of checks, microfilms of all cancelled checks and microfiche indices of the microfilms,

(7) Telegraph transfer services, and

(8) Foreign exchange services.

In order to facilitate the State's investment program, each working day at 8:15 a.m. the bank must notify the state treasurer of the collected balance in the State's account in order that short-term investments can be made that day. A monthly account analysis will be provided showing the average daily balance and the resulting excess or deficit position in compensating balances.

Banks and the Selection Process

As noted above, the state working bank is selected by the investment board from among those Wisconsin commercial banks which prepare and submit a proposal for the State's account. Not all banks are anxious to have the State's account. The volume is great and it will have a significant impact on the bank's operations. Obviously only a large bank with a highly computerized transit department could handle the very large volume of work generated by the state account. If the bank doesn't have accurate information about its internal costs, income from this account may not cover the costs associated with servicing it. Another important consideration is what happens when the account is shifted again in 6 to 12 years as seems entirely likely. Since the addition in demand deposits resulting from the State's account are substantial, it may be necessary to increase the bank's capital structure. Finally, potential bidders must consider what, if any, effect serving as the state working bank will have on other large bank customers (e.g., will these customers want banks to bid for their account?).

On the other hand, both state officials and bankers believe there is some prestige in being the State's banker. Banks might also see this as an opportunity to make new contacts and possibly as an opportunity to further develop certain banking functions that previously had received too little attention. Undoubtedly, however, the chief reason Wisconsin's banks would consider bidding for the State's account is to increase profits.

Competing banks' proposals are submitted in terms of compensating balances that the State must keep in demand deposits at the working bank. The State provides information on the type and volume of services needed. Each bank details the costs of handling the State's banking business and indicates what compensating balance is required to cover these costs including whatever profit the bank considers appropriate. Appendix B is the proposal form devised by the Wisconsin Investment Board.

Table 3 illustrates the computation of costs and their relationship to compensating balances. In this hypothetical one-month period, the State's balance exceeded the minimum required balance so the resulting excess is credited to the following month. In instances where the State's balance was below that needed to cover the costs of administering the account, the deficit would be made up in the following month.

Again, in the Table 3 illustration, a deficit would occur if the monthly direct charges had exceeded $52,016 or if the compensating balance had been at a level such that the interest credit (102 percent of the treasury bill rate) was less than $48,705, or some combination of both.

Table 3

Example of Compensating Balance Credit Calculations

Total Monthly Direct Charges	$ 48,705
Average Collected Balance in the State's Account During the Month	10,618,300
Less 12 percent Federal Reserve Requirement	1,274,196
Net Collected Balance	$ 9,344,104
Interest Credit Computed at 102 percent of the Average Treasury Bill Rate (6.55 percent) for the month[a] (102 percent x 6.55 percent = 6.68 percent x $9,344,104 ÷ 12 =	$ 52,016
Excess Credit ($52,016 - $48,705) available to apply to subsequent month's charges	$ 3,311

[a] *102 percent of the average treasury rate is the credit rate determined by the State and the bank through the "bid" process.*

Source: *State of Wisconsin, "Specifications for Proposals to be the State Working Bank," Appendix B, October 15, 1975.*

In addition to providing the services listed previously, it is the view of investment board staff that the state working bank should have deposits of at least $120 million and that its capital, capital notes, surplus, undivided profits, and reserves equal at least $11 million.[32]

Questions that might be asked are, "Is the investment board the most appropriate agency to select the state working bank?" and "Does the selection procedure insure that the State gets the best possible deal?"

Regarding the first question, it is true that on a day-to-day basis both the treasurer and the Department of Administration have more extensive dealings with the state working bank than the board. The procedures developed will affect these agencies most directly, and the board has no particular expertise in developing the needed cash management, auditing, or accounting systems.

No compelling case can be made for an independent investment board's selecting the state working bank. Nevertheless, in Wisconsin the board's independent status, its arms-length review of proposals, and its generally good reputation lend considerable credibility to the selection process. Moreover, the trustees have financial and investment expertise, solicit the ideas of the treasurer's office and the Department of Administration in developing the specifications, and seek the advice of their custodian bank in New York City in evaluating the proposals.

Whether or not the State is getting the lowest possible costs as reflected in the required compensating balance is not known. However, the bidding procedure would seem to assure a reasonable charge for services. State officials appear satisfied. The response by the Wisconsin state treasurer is believed representative:

> ". . .under the State of Wisconsin philosophy of securing bids to serve as the state depository, we feel that the bidding banks through competition will arrive at a proper cost factor for their services. As a matter of truth we would be very reluctant to impinge our limited knowledge of bank costs upon banks who should bid on the basis of their own particular costs plus a reasonable profit.[33]

Again, this is not to suggest that the investment board is precluded from reviewing the bank's range of services, professional staff, equipment and facilities to ascertain if the bank can provide a proper level of services.

Utilizing the State Working Bank in Other States

In most States, the greatest obstacle to implementing the single state working bank concept is political. In Wisconsin the state working bank has been in operation for over 20 years and is generally accepted by Wisconsin's bankers. As taxpayers and businessmen it is difficult for banks and bankers to argue with the substantial efficiency savings and investment earnings.

Needless to say, the State's bankers have not always been so sanguine where the single depository for state money is concerned and as noted in the previous section, they opposed the creation of the local government investment funds. Perhaps the rationale most frequently advanced for maintaining numerous state accounts is the economic development one: these state dollars are used by local banks to generate additional business in the region. The viewpoint expressed by Wisconsin's elected treasurer seems appropriate:

> "Up to this time (although I admit there is considerable pressure to the contrary) the State of Wisconsin, the Investment Board specifically. . .subscribes to the philosophy that money is a free-flowing object of trade that ignores political boundaries, and that attempts to promote local or regional business through bank de-

posits is to little avail. We tend to feel that generally such deposits are merely invested by the receiving bank in that form of investment which will realize to that bank the greatest income.[34]

In other words, many investment officials do not accept the economic development argument since local government funds will be used wherever the bank can obtain the highest rate of return—usually not in the local economy unless it is expanding rapidly. Furthermore, a number of States require that banks must put up collateral as security for state deposits. For instance, in Kentucky; banks must post government securities worth 110 percent of the uninsured portion of the deposit. Consequently, the result of these "linked deposits" in Kentucky is that state deposits of public funds in commercial banks may reduce the amount available to promote economic expansion. Recently, South Dakota dropped the collateral requirements on state deposits from 100 percent to 5 percent potentially "freeing up" an estimated $180 million in South Dakota banks for other investments and loans.

The local economy and town residents, in fact, may benefit precisely because local funds are temporarily withdrawn from local banks in order to obtain a better interest rate elsewhere, such as through investments in the State's local government pooled investment fund.

From the standpoint of being able to engage banks that can provide the necessary services, a State's largest banks probably will bid to become the state working bank. Since the size of state government and the size of banks are both somewhat related to population, it seems likely that within each State there are banks that could handle the State's business. The banks in Wisconsin that bid on the state account have total deposits of $1,859,678,000 (First Wisconsin) and $581,525,000 (Marshall & Ilsley). This makes them the 48th and 161st largest banks in the country, suggesting that banks of varying size can handle the state account.[35]

While Wisconsin uses only one bank, it would be possible, if slightly more difficult, to use more than one working bank. For example, South Dakota uses two banks and alternates each month. A thorough analysis of the services required and volume of transactions within various state accounts would reveal the complexity involved.

In branch banking States, it might even be easier to implement the state working bank concept since transactions could be made throughout the State with immediate accounting. Collections and cash disbursements would occur more rapidly.

VI. TRANSFERRING THE WISCONSIN PROGRAM

Some innovative state government programs are not applicable to many other States. This one is. It is not associated with size or composition of population, rural/urban considerations, size of State, geography, or the State's fiscal condition. All States collect large amounts of money and expend large amounts of money; therefore they have an enormous cash flow. All States have significant amounts of cash that are not needed for payments on any particular day and which, therefore, could be earning interest.

The review of the Wisconsin investment program suggests that the administrative factors are probably less important than the political ones in precluding the transfer of this comprehensive investment program from one State to another. The two groups most adversely affected appear to be bankers and existing boards, agencies, or councils which are responsible for investing various public funds. The latter group simply will not want to have this important investment responsibility transferred from it to a centralized investment board. The reasons are easily deduced and don't require expansion here. Bankers naturally will not like losing the earnings from the deposits of the State. The combination of establishing a state working bank, investing the check float, creating a local government investment pool, and investing idle cash balances are all programs that result in greater earnings for government at the expense of banks. In the case of both centralized banking and centralized investing the benefits to government can easily be measured.

Opposition may also come from the state treasurer since a comprehensive investment program probably will mean the treasurer's loss of some control of these funds. In Wisconsin, for example, the Department of Administration, not the treasurer, operates the computer system and performs the data processing and accounting. The investment board and staff make all the investment decisions.

Legal Issues

State investment policies are influenced by the institutional setting in which investment policy is developed and by the philosophy and investment goals of various policymakers, but all of these factors are circumscribed by the constitutional, statutory, and administrative guidelines of the individual States.

In numerous States, the laws are silent on many matters affecting the development of a comprehensive investment program. Such was the case in Wisconsin and interpretations of the statutes generally have been strict in findings that necessitate specific statutory provisions authorizing board activities—the municipal investment pool, the investment of float, expanding the types of instruments that can be used for investment purposes, and the use of a custodian bank in New York City to physically hold and transfer securities.

There are other instances where the statutes limit the number and types of securities which may be held in the portfolio, the time periods an investment may be held, or the amount of treasury balances that may be invested. The use of banks as holding institutions for treasury balances when the money is not invested may also be subject to statutory limitation.

Equally as important as the statutes or administrative guidelines are the administrative procedures and policies (sometimes spelled out in law) that greatly affect the potential for cash management. Wisconsin has a system of centralized cash disbursement; rapid and centralized collections through lock boxes; one bank account; regulations requiring agencies to transfer funds immediately to the treasury; a centralized uniform accounting system, and a sophisticated, centralized, computer system. This centralized management capacity is lodged in a Department of Administration which has considerable authority over management systems and reports as well as budgeting and personnel. These factors certainly facilitate the development of a comprehensive state investment program. As the Wisconsin case shows, developing an extensive investment program can occur in stages with an investment board, followed by a working bank(s), and sophisticated accounting and computer systems, flexibility in investment instruments, and a custodian bank.

Another major component in the present program is competent staff to manage over $2 billion in assets. However, the market for investment professionals is a national one, so it should not be difficult to attract personnel if reasonably competitive salaries are offered. It has been suggested that many state capitals offer pleasant living environments that many prospective employees would find desirable.

An equally important issue is whether outside consultants should manage state investments or whether this important activity should be conducted by state employees. While States may wish to divide investment operations between government and nongovernment employees for a period of time to determine which group achieves greater success, several items suggest that in-house investment may be the preferable course. First, responsibility for state investment operations should be assumed by a state official who can be rewarded or disciplined based on performance. With delegation of this responsibility to an outside firm, there is less control of personnel, and little redress for poor investment performance except dismissal of the firm. Secondly, if state officials invest state funds, they are investing some of their own retirement and tax funds, a procedure which is different than investing someone else's funds. Thirdly, and perhaps most importantly, in-house investment salary costs (for an equivalent level of service) will nearly always be significantly less than private firms' salaries. If this differential in salaries could be offset by higher investment returns from private consulting firms, there would be no problem. Private consulting services, however, have not consistently produced better investment yields than state investment officials. Finally, in-house investing has no administrative marketing or advertising expense.

In sum, if the political obstacles can be overcome and translated into satisfactory legislation, then any State can begin developing the computer and accounting programs and banking relationship needed to pursue an efficient investment program. The State of Wisconsin appears to be managing its cash flow in such a way as to permit maximum investment opportunity. There are no idle cash balances in Wisconsin, only a compensating balance to pay for bank services. There are very few unutilized or unauthorized investment channels.

In conclusion, the modifications described in this report, almost always mandated by specific statute, have resulted in an investment process in Wisconsin that can serve as a model for other state officials in evaluating their investment practices.

FOOTNOTES

1. Derived from data presented in State of Wisconsin Investment Board

1. Derived from data presented in State of Wisconsin Investment Board *Annual Report* for fiscal year ending June 30, 1975. p. 6.

2. *Annual Report*, p. 8.

3. The Legislative Audit Bureau reports that some state departments have a few small working or contingent checking accounts which are restricted for specific payments.

4. Interdepartmental memo to Pat Hays, Bureau of Budget and Planning, from Peter J. Nelson, Assistant State Treasurer, November 28, 1975.

5. Interdepartmental memo to Pat Hays from Ken Engle, dated December 11, 1973.

6. Investment Board, "Manual of Functions, Goals, Policies, and Procedures," October 15, 1974.

7. Both amounts represent increases provided in 1975 Assembly Bill 222, Sections 256 and 257, respectively.

8. The investment board addresses the social responsibility issue in its *Annual Report* for fiscal year ending June 30, 1975, pp. 19-20.

9. See State of Wisconsin Investment Board, "Manual of Functions, Goals, Policies, and Procedures," October 15, 1974.

10. A number of restrictions have been placed on the private financial transactions of board employees to prevent unethical behavior. No employee, including support personnel, may purchase a new stock or bond offering until it has traded on one of the financial markets. In addition, a board employee cannot buy issues of a company at the same time as the board is adding the issue to its portfolio unless the employee can demonstrate a long-term continuous pattern of purchasing the specific issue. Furthermore, each investment director must file with the executive director a quarterly report listing all equity transactions. Finally, all board employees' federal tax returns must be submitted with the Wisconsin state tax return, and state returns are audited annually.

11. *Annual Report*, p. 13.

12. *Annual Report*, p. 18.

13. "Manual of Functions, Goals, Policies, and Procedures," page 11. It is also policy of the board that "no investment shall be made in stocks of companies which sell as a substantial product line tobacco, liquor, or gambling."

14. Interview with James Severance, May 14, 1976.

15. See "Background and Operations of the Private Placement Division," a paper prepared by Robert Zobel, Investment Director for Private Placements.

16. By policy of the board, no private placements are made in tobacco and alcohol firms or in real estate investment trusts. Few placements have been made in the insurance, finance, and medical fields because of limited staff experience with those areas. Normally preference will be given to loans which generate new jobs through capital expansion if the return is nearly equivalent to other loan applications. No distinctions are made according to characteristics of either the owner or company product line except those noted above.

17. Nor may the placements division entirely own a firm, a policy adopted by the board's trustees. Trustees, however, will permit the division director to sit on boards of directors of various companies. As the largest lender to many smaller firms, it would be appropriate for the investment board to be given a board seat. The current division director has decided not to become a member of any boards because of time constraints.

18. See the 1975 *Annual Report*, pages 9, 10.

19. It is understood that much of this section of Wisconsin law was derived from New York Statutes (Chapter 260, Section 34).

20. The 9.02 percent return on an average daily balance in fiscal 1974 of $662 million earned $5.9 million for the State. In fiscal 1975, $54 million was generated.

21. According to investment agency officials, Wisconsin is one of a few States that uses the reverse repurchase agreement. The South Dakota Investment Council, also a sophisticated state investment agency, has arranged double-reverse repurchase agreements. In contrast to other state governments, the investment board normally does not invest heavily in bank certificates of deposit. Certificates of deposit (CD's) limit investment flexibility because their rates are established for a given time period, thereby preventing investment officials from taking advantage of fluctuating interest rates on other investments. Also, because CD's are not collateralized, CD's are not easily transferred in the national market.

22. Readers should note that the board's tax-exempt status is not the primary reason for its lower administrative expenses. In Table 2 the asset/expense comparison was computed with taxes excluded.

23. The Wisconsin legislation was modeled after a 1973 local government investment program enacted in Oregon. In Oregon the program was available at first only to county governments and larger cities. Presently, the majority of local governments in Oregon are participating in the program, and the level of local funds has expanded from $100 million to over $400 million.

24. The investment board has not yet established criteria (such as minimum times for investments, types of investments, and restrictions on number of purchases) for the trust fund.

25. Memo from Peter Nelson, Office of the Wisconsin State Treasurer, July 1976.

26. The Department of Administration anticipates that a monthly letter will be distributed to local officials whose cities have funds in the pooled fund. However, it is unlikely that specific investments will be identified.

27. In South Dakota, for example, state funds are rotated each month between two banks, and a South Dakota official estimated that this costs the State one day's interest on $5 million each month—or over $8,000 per year (assuming a 5 percent interest rate and a 360-day year).

28. From 1958 to 1964 the state working bank was First Wisconsin National Bank of Milwaukee; 1964 to 1976 the Marshall & Ilsley Bank (Milwaukee); and in 1976 First Wisconsin is the state working bank. Only these two banks bid on the state account although it has been suggested five or six Wisconsin banks are large enough to handle the State's account.

29. These volume figures are reported in an investment board staff memo to the trustees dated June 17, 1975. The number of deposit items was provided by Peter Nelson, Office of the Treasurer.

30. Washington State adopted a lock box procedure for all state tax remittances in mid-1975. At that time, the Department of Revenue anticipated a reduction in collection costs of $60,000 annually and increased earnings of over $340,000 a year based on additional investment through quicker tax collection. The bank involved handles the deposits without charging the State a fee.

31. Taken from a 10-page memorandum (plus appendices) prepared by the State of Wisconsin Investment Board entitled "Specifications for Proposals to be the State Working Bank," dated October 15, 1975.

32. Memo to trustees from the staff's State Working Bank Committee, dated June 17, 1975.

33. Letter from Charles P. Smith, Wisconsin State Treasurer, to Jack Kiley, Administrative Assistant to the State Treasurer of Washington, dated July 19, 1972.

34. Wisconsin State Treasurer Charles P. Smith, letter to Jack Kiley.

35. Based on information compiled by the *American Banker*, 525 West 42nd Street, New York City. Data are for June 30, 1975.

APPENDICES

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STATE OF WISCONSIN

1975 Senate Bill 788 — Date published*: February 20, 1976

CHAPTER 164 , LAWS OF 1975

AN ACT to amend 20.906 (1) and (5), 34.01 (intro.), (1) and (8) (a), 59.75 (1) and 66.04 (2); and to create 16.53 (10) and (11), 20.002 (11), 20.855 (8), 20.906 (6), 25.17 (1) (jg) and (jr), 25.50, 25.55 and 59.74 (2) of the statutes, relating to state treasury cash flow management, establishing a local government pooled-investment fund and a local government trust-investment fund and granting rule-making authority.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

SECTION 1. 16.53 (10) and (11) of the statutes are created to read:

16.53 (10) PRIORITY OF CLAIMS. If, between the effective date of this act (1975) and 30 days after the publication of the budget adopted for the 1977-79 fiscal biennium, an emergency arises which requires the department to draw vouchers for payments which will be in excess of available funds in any state fund, the secretary, in consultation with the state treasurer and the joint committee on finance, may prorate and establish priority schedules for all payments, including those payments for which a specific payment date is provided by statute. The secretary shall draw all vouchers according to the following preference. All direct or indirect payments of principal or interest on state bonds and notes have first priority and may not be prorated or reduced under this subsection. All state employe payrolls shall have 2nd priority. All payments to local units of government which are required by statute to be made on a specific date and all aid payments to individuals have 3rd priority. All remaining payments have 4th priority. The secretary shall maintain records of all claims prorated under this subsection and shall provide written notice to the state treasurer when a potential cash flow emergency is anticipated.

(11) INTEREST ON PRORATED PAYMENTS. Payments prorated under sub. (10) which are payable to local units of government shall earn interest on the daily unpaid balance at the rates of interest earned by the state investment fund during the calendar quarter in which the proration occurred. The interest payments under this subsection shall be credited to the respective local units of government at the end of the quarter in which the proration occurred.

SECTION 2. 20.002 (11) of the statutes is created to read:

20.002 (11) TEMPORARY REALLOCATION OF SURPLUS GENERAL FUND APPROPRIATIONS. All appropriations and special accounts within the general fund may be made temporarily available for the purpose of allowing encumbrances or financing expenditures of other general fund activities which do not have sufficient funds in their account but have accounts receivable balances. The secretary of administration shall determine the composition and allowability of the accounts receivable balances for this purpose and shall specifically approve the use of surplus general funds for use by specified activities or programs. The secretary may assess a special interest charge against the programs or activities utilizing surplus funds under this subsection in amounts not to exceed the daily interest earnings rate of the state investment fund during the period of transfer of surplus funds to other accounts or programs.

SECTION 3. 20.855 (8) of the statutes is created to read:

20.855 (8) PAYMENTS TO LOCAL UNITS OF GOVERNMENT. (a) *Interest on prorated payments.* A sum sufficient to pay interest on payments to local units of government under s. 16.53 (11).

SECTION 4. 20.906 (1) and (5) of the statutes are amended to read:

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*Section 990.01, Wisconsin Statutes: Laws and acts; time of going into force. "Every law or act which does not expressly prescribe the time it takes effect shall take effect on the day after its publication."

20.906 (1) FREQUENCY OF DEPOSITS. Unless otherwise provided by law, all moneys collected or received by any state agency for or in behalf of the state, or which is required by law to be turned into the state treasury, shall be deposited in or transmitted to the state treasury at least once a week and also ~~whenever~~ at other times as required by the governor, or the state treasurer and shall be accompanied by a statement in such form as the treasurer may prescribe showing the amount of such collections and from whom and for what purpose or on what account the same was received. All moneys paid into the treasury shall be credited to the general purpose revenues of the general fund unless otherwise specifically provided by law.

(5) CONDITIONS PRECEDENT TO RELEASE OF APPROPRIATIONS. All appropriations ~~made by law~~ from state revenues for any state agency, are made on the express conditions that such state agency pays all moneys received by it into the state treasury within one week of receipt or as often as otherwise directed by the governor or state treasurer, and conforms with ss. 16.53 (1) and 20.002, both as to program revenue and general purpose revenue appropriations from all funds. Upon failure to comply with the above conditions, the department of administration shall refuse to draw its warrants, and the state treasurer shall refuse to pay any moneys appropriated to the state agency from state revenues, until compliance is made with said conditions ~~and upon~~. Upon failure or refusal to so comply, after due notice received from the department of administration, any appropriations ~~made by law~~ from state revenues to the state agency shall permanently revert to the fund from which appropriated.

SECTION 5. 20.906 (6) of the statutes is created to read:

20.906 (6) DIRECT DEPOSITS. The governor or the state treasurer may require state agencies making deposits under this section to make direct deposits to a bank designated as a depository by the state investment board, if such a requirement is advantageous or beneficial to this state.

SECTION 6. 25.17 (1) (jg) and (jr) of the statutes are created to read:

25.17 (1) (jg) Local government pooled-investment fund (s. 25.50);

(jr) Local government trust-investment fund (s. 25.55);

SECTION 7. 25.50 and 25.55 of the statutes are created to read:

25.50 Local government pooled-investment fund. (1) DEFINITIONS. In this section:

(a) "Board" means the state investment board.

(b) "Fund" means the local government pooled-investment fund.

(c) "Local funds" means funds under the control or in the custody of any local government or local official that are not required to meet current expenditures or demands.

(d) "Local government" means any county, town, village or city in this state.

(e) "Local official" means each officer or employe of a local government who by law or vote of the governing body of the local government is made the custodian of funds.

(2) CREATION. There is established within the state investment fund a local government pooled-investment fund with a separate and identifiable account within the fund for each local government.

(3) LOCAL GOVERNMENTS AUTHORIZED TO PLACE FUNDS IN FUND. (a) With the consent of the governing body, a local official may transfer local funds to the state treasurer for deposit in the fund.

(b) On the dates specified and to the extent to which they are available, subject to s. 16.53 (10), funds payable to local governments under ss. 70.996 (1) (a), 79.02 (2) (a), 79.03 (1), 79.04 (1), (2) (a) and (3), 79.05 (2), 79.055, 79.06, 79.08, 79.10 (1) and (3) and 79.17 (1) and (3) shall be considered local funds and, pursuant to the instructions of local officials, may be paid into the separate accounts of all local governments established in the local government pooled-investment fund and, pursuant to the instructions of local officials, to the extent to which they are available, be disbursed or invested.

(4) PERIOD OF INVESTMENTS; WITHDRAWAL OF FUNDS. Subject to the right of the local government to specify the period in which its funds may be held in the fund, the state treasurer shall prescribe the mechanisms and procedures for deposits and withdrawals.

(5) INVESTMENT POLICIES. The investment board shall formulate policies for the investment and reinvestment of moneys in the fund and the acquisition, retention, management and disposition of such investments.

(6) INVESTMENT BOARD TO INVEST, REINVEST POOLED FUNDS. In the amounts available for investment purposes and subject to the policies formulated by the investment board, the investment

board shall invest and reinvest moneys in the fund and acquire, retain, manage, including the exercise of any voting rights, and dispose of investments of the fund.

(7) REIMBURSEMENT OF EXPENSES. The state treasurer shall deduct quarterly a maximum of 0.25% of the amount of income received from the earnings of the fund during the preceding calendar quarter for all actual and necessary expenses incurred by the state in administering the fund.

(8) SEPARATE ACCOUNTS. (a) The department of administration shall keep a separate account for each local government and shall record the individual amounts and the totals of all investments of each local government's moneys in the fund.

(b) The state treasurer shall report monthly to each local official the deposits and withdrawals of the preceding month and any other activity within the account.

25.55 Local government trust-investment fund. (1) There is created a local government trust-investment fund under the jurisdiction and management of the investment board.

(2) Local governments as defined in s. 25.50 (1) (d), may transfer to the state treasurer for deposit in the local government trust-investment fund excess cash for investment by the investment board. Local governments shall specify the term of investment of moneys transferred. The department of administration shall set up a separate account for each local government. The investment board shall invest each account separately in investments authorized under s. 25.17 (3) (b), (ba) and (dg). All interest accruing as a result of such investment shall be allocated to the account for which it was invested. The investment board shall prescribe rules determining the amounts which may be transferred to this fund for investment and the procedures to be followed for making deposits and withdrawals.

(3) Administrative expenses allocated to the operation of this fund shall be deducted from interest earned by the fund in an amount not to exceed 0.25% per quarter of the interest earned by the separate accounts in the fund.

SECTION 8. 34.01 (intro.), (1) and (8) (a) of the statutes are amended to read:

34.01 Definitions. (intro.) ~~As used in~~ In this chapter:

(1) "Public deposit" ~~shall mean~~ means moneys deposited by the state or any county, city, village, town, drainage district, power district, school district, sewer district, or any commission, committee, board or officer of any governmental subdivision of the state, or any court of this state, in any state bank, savings and trust company, mutual savings bank, or national bank in this state or in the local government pooled-investment fund or the local government trust-investment fund, including private funds held in trust by a public officer ~~for persons, corporations or associations of individuals~~.

(8) (a) "Inactive deposits ~~shall mean~~ means public deposits which have been deposited subject to the bank's rules and regulations relative to time accounts and the investment board's rules relative to amounts invested in the local government trust-investment fund.

SECTION 9. 59.74 (2) of the statutes is created to read:

59.74 (2) In addition to the depositories specified in sub. (1), the local government pooled-investment fund and the local government trust-investment fund may be designated as depositories for investment purposes.

SECTION 10. 59.75 (1) of the statutes is amended to read:

59.75 (1) Whenever any county board ~~shall have~~ has designated a county depository ~~or depositories in accordance with the provisions of section~~ under s. 59.74 the county treasurer shall deposit therein as soon as received all funds that come to ~~his~~ the treasurer's hands in that capacity in excess of the sum ~~he~~ the treasurer is authorized by ~~such~~ the board to retain ~~and any~~. Any sum so on deposit shall be deemed to be in the county treasury, and ~~such~~ the treasurer shall not be liable for any loss thereon resulting from the failure or default of such depository~~; provided, that the~~. The county board or a committee thereof designated by it may invest any funds that come into ~~his~~ the county treasurer's hands in excess of the sum ~~he~~ the treasurer is authorized by the county board to retain for immediate use, in the name of the county in the local government pooled-investment fund, in the local government trust-investment fund or in ~~interest-bearing~~ interest-bearing bonds of the United States, or of any county or municipality in the state~~, and such~~. The board or committee may sell such securities when deemed advisable.

SECTION 11. 66.04 (2) of the statutes is amended to read:

66.04 (2) INVESTMENTS. Any county, city, village, town, school district, drainage district, vocational, technical and adult education district, or other governing board as defined by s. 34.01 (4) may invest any of its funds, not immediately needed, in time deposits in any bank, savings bank or trust company which is authorized to transact business in this state, such time deposits maturing in not more than one year, or in bonds or securities issued or guaranteed as to principal and interest of the U.S. government, or of a commission, board or other instrumentality of the U.S. government, or bonds or securities of any county, city, drainage district, vocational, technical and adult education district, village, town or school district of this state, or, in the case of a town, city or village, in any bonds or securities issued under the authority of such municipality, whether the same create a general municipality liability or a liability of the property owners of such municipality for special improvements ~~made thereon~~, and may sell or hypothecate the same. Any county, city, village or town may also invest surplus funds in the local government pooled-investment fund or the local government trust-investment fund. Cemetery perpetual care funds, pension funds under s. 62.13 (9) or (10), or endowment funds including gifts where the principal is to be kept intact may also be invested under ch. 881.

SECTION 12. **Program responsibilities.** (1) In the list of program responsibilities enumerated for the office of the state treasurer in section 14.561 of the statutes, insert references to sections "25.50" and "25.55".

(2) In the list of program responsibilities enumerated for the department of administration in section 15.101 (intro.) of the statutes, insert reference to sections "25.50" and "25.55".

(3) In the list of program responsibilities enumerated for the investment board in section 15.761 of the statutes, insert reference to sections "25.50" and "25.55".

SECTION 13. **Cash flow study.** The department of administration is directed to prepare a report on the present statutory and administrative structure and procedure for the payment of local assistance funds to counties, towns, villages, cities and school districts. The report, after review by a 7-member committee consisting of the state treasurer, representatives of the departments of administration and public instruction, and designees appointed by the league of Wisconsin municipalities, county boards association, Wisconsin towns association and the Wisconsin school boards association, shall be submitted to the governor and the legislature no later than February 1, 1977, and shall include but not be limited to:

(1) The identification of major local assistance payments.

(2) The identification of payment schedules either required by statute or established by administrative action.

(3) An assessment of the impact of such payments and schedules on fund balances and the operation and management of the state budget.

(4) The criteria on the basis of which the current payment schedules were established.

(5) The impact of current payment schedules on the operation of local and state government.

(6) Recommendations, if deemed appropriate, for changes in the statutes or in administrative procedures concerning such payments and schedules.

PROPOSAL FORM TO BE
THE STATE OF WISCONSIN WORKING BANK

To: State of Wisconsin Investment Board

The following constitutes our proposal to provide the State of Wisconsin's banking business requirements for the period commencing July 1, 1976, and terminable on our part by giving one year's notice.

It in understood that, should our proposal be accepted, we will be designated as (1) State Working Bank, and (2) a State depository bank pursuant to the provisions of s. 25.17 (61), Wisconsin Statutes.

It is further understood that the State of Wisconsin Investment Board, in its sole discretion, may reject this or any other proposal.

In addition, this bank agrees that the Investment Board may exclude any specific service or element thereof in any contract which may result from this proposal.

OFFER

This bank offers to provide all of the services outlined in that certain set of specifications dated October 15, 1975 and labeled "Specifications for Proposals to be the State Working Bank."

This bank agrees that it will maintain dormant balances, as directed, in designated banks for the benefit of the state. In consideration, an identical amount shall be subtracted from the net collected balance before applying the compensating balance formula outlined on page 6 of this proposal.

This bank agrees that it will establish and maintain a $10 million open line of credit and allow draws against such line by the Wisconsin Building Commission on the condition that any draw against the line of credit shall bear interest at the rate of

_____%

of the bank's prime rate as posted from time to time.

-1-

-2-

TIME SCHEDULE UNDER WHICH
THIS BANK WILL CREDIT THE STATE TREASURER'S
ACCOUNT WITH COLLECTED FUNDS

This bank agrees that all deposits delivered during any working day to it or its Madison Agent, if any, will be credited to the State Treasurer's account as though they had been delivered to the Milwaukee Branch of the Federal Reserve Bank on that same day.

In addition this bank agrees that it will credit the State Treasurer's account with collected funds earlier than the Milwaukee office schedule on the following:

	When Credited (Same day, 1 day deferred)
c	

This bank will provide the following system for check retrieval and copying for the Treasurer's Office and our time table for making it available is as follows:

1. System Description

2. Time Table

COMPENSATION

This bank agrees to provide the services as specified for the following direct (hard dollar) charge per item:

Item	Dollars per item
1. Deposit Items	
(a) Per local deposit item	$ _____
(b) Per transit deposit item	$ _____
(c) Per N.S.F. item	$ _____
(d) Blank Deposit tickets - per 1000	$ _____
(e) Coupon Interest Collection Service per coupon	$ _____
(f) Wisconsin G.O. Bond Coupons per presentation	$ _____
2. Ledger Items	
(a) Deposit ticket or credit memo - each	$ _____
(b) Per check drawn on us	$ _____
3. Other Checking Services	
(a) Blank Checks	
(1) Series A,C,D,E,F,H, and R per 1000 checks	$ _____
(2) Series B - per 1000 checks	$ _____
(3) Series G,I, and X - per 1000 checks	$ _____
(b) Reconciliation - per item	$ _____
(c) Storage boxes - each	$ _____
(d) Microfilming checks for Treasurer's use - per check	$ _____
(e) Microfiche index for Treasurer's use per microfiche	$ _____
(f) Microfiche images of computer printouts - per microfiche	$ _____

4. Lockbox Services

(a) Withholding

(1) Employers deposit report form - each $ _____

(2) Microfilming report form - each $ _____

(b) Motor and Special fuel

(1) Motor fuel report form - each $ _____

(2) Special fuel report form - each $ _____

(3) Microfilming report form - each $ _____

5. Wire Transfer Services

(a) Federal Wire - each $ _____

(b) Bank Wire - each $ _____

(c) Telephone advice - each $ _____

6. Securities Clearance Services

(a) Transaction - each $ _____

7. Government Bond Services

(a) per Bond $ _____

8. Transportation Services

(a) Cash pick-up from State Treasurer's Office, Madison - per trip $ _____

(b) Deposit pick-up from Department of Revenue, Milwaukee - per trip $ _____

(c) Pick-up and delivery of various items (checks, deposits, cancelled check, microfilm, etc., no cash) round trip from Working Bank to Madison offices of State Treasurer, Department of Revenue, and Department of Transportation per round trip $ _____

(d) Special Courier runs

(1) Federal Reserve Bank, Chicago - per trip $ _____

(2) Chicago Loop Banks - per trip $ _____

COMPENSATING BALANCES
IN LIEU OF DIRECT CHARGE

In lieu of a direct charge for the services referred to above, this bank agrees that it may be compensated by collected balances in the State Treasurer's account.

The bank agrees to credit as payment for such charges an amount equal to one day's interest (computed on a 360-day year) using an interest rate equal to

_____%

of the monthly average of the 90 (91-92) day U.S. Treasury Bill rate* on each dollar of collected balances (less reserve requirements of the Federal Reserve Bank) left on hand each day during the month in the State's account.

*as reported in the Moodys Bond Survey

In the event that the application of this formula produces a credit in excess of monthly charges, the bank agrees to apply such excess as credit towards the following month's charges. Conversely, the State will make up any deficit by increasing balances the following month.

Dated this ____ day of _____, 1975.

Name of Bank: _____

By: _____

Title: _____

Attest: _____

Title: _____