



State of North Carolina

Department of State Treasurer

RICHARD H. MOORE
TREASURER

*State and Local Government Finance Division
and the Local Government Commission*

Memorandum # 1094

December 20, 2007

To: Finance Officers of Local Governments, Boards of Education, Public Authorities
and Certified Public Accountants

From: Sharon Edmundson, Director Fiscal Management Section

Subject: Collateralization of Public Deposits and Pooling Bank List

On the 3rd page of this memo you will find a list of the financial institutions using the Pooling Method of collateralizing public funds at December 31, 2007. The State Treasurer monitors compliance with collateralization requirements for these institutions. Any depository (and their branches) not included on this list is considered to be using the Dedicated Method of collateralization for which the finance officer has the responsibility of monitoring the pledged collateral covering the uninsured deposits. **Please review the list carefully to determine the method currently used by each of your official depositories.**

For situations where a financial institution utilizes the Dedicated Method of collateralization, the finance officer should determine that the market values of the pledged securities are at least 100% of the amount required to be collateralized at all times throughout the year and that the securities are eligible for pledging as specified by the North Carolina Administrative Code, Title 20, Chapter 7. It is imperative that the market values of the pledged securities are checked not only at the time of the deposit of public funds, but on a continuing basis when funds exceed the federal deposit insurance limit. This is essential due to the volatility of the pledged securities' market value and the fluctuation of the unit's bank balances. Any occurrence of under collateralization is considered as non-compliance with G.S. 159-31.

For eligible mortgage-backed securities that are pledged as collateral, the calculation of market values is more difficult due to their declining principal balances. The calculation of the market values of such securities should be based on the outstanding principal value, not the original face value. Therefore, it is important to require the depository to provide a) the original face value b) the current outstanding principal and c) the current market value.

In addition, there are mandatory procedures concerning collateralization that must be followed when dealing with Dedicated Method financial institutions. They are as follows:

1. There must be a signed escrow agreement (INV-94) with a third party escrow agent for each Dedicated Method depository that holds uninsured deposits. However, if the escrow agent is the Federal Reserve Bank, an escrow agreement is not required since they are governed by federal regulations. The escrow agreement (federal regulations in the case of the Federal Reserve Bank) must require timely confirmations of pledged collateral.
2. A file of all pledges of collateral (INV-95) per depository must be maintained by the finance officer. There should be no releases or substitutions of collateral securities resulting in a decrease of the market value of pledged securities without the approval of the finance officer.
3. The depository is required to report to each public depositor the total par and market values of securities pledged at the end of each calendar quarter. Annually, as of June 30, it is to file with each public depositor an INV-98. This report is a detailed listing of collateral securities pledged at each escrow bank for that public depositor. This report may be requested by the public depositor to be filed more frequently.

Without exception, if governmental units utilizing the dedicated method of collateralization do not adhere to these procedures, public funds may not be properly collateralized and consequently may be at risk.

For more detailed information, the complete regulations, procedures, and the respective N.C. Administrative Code can be found in a document called "Collateralization of Public Deposits in North Carolina," January 2001. It can be downloaded from the State Treasurer's web site at <http://www.nctreasurer.com/> under Financial Operations. The appropriate forms are also available from the same web page. If the booklet or forms are needed and cannot be retrieved from the web, you may contact this office. If you have any questions or need assistance, please call Samantha Carter at 919 807 2396 or email samantha.carter@nctreasurer.com .

