



**House
Legislative
Analysis
Section**

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**ALLOW ELECTRONIC TRANSFER
OF LOCAL GOVERNMENT FUNDS**

**House Bill 6496 (Substitute H-1)
First Analysis (12-3-02)**

**Sponsor: Rep. Marc Shulman
Committee: Local Government and
Urban Policy**

THE APPARENT PROBLEM:

The automated clearing house (ACH) network is a nationwide electronic funds transfer system that processes electronic payments for financial institutions. Individuals, businesses, and governments, acting through their financial institutions, originate and receive electronic payments, and the ACH operator acts as a go-between by processing or “settling” the transfer of funds. Examples of ACH payments include direct deposit of payroll, direct bill payments, and e-checks. According to the National Automated Clearing House Association, the value of ACH payments was \$22.2 trillion in 2001 alone. Perhaps more significantly, nearly 8 billion payments were made in 2001, a 16.2 percent increase over the volume in 2000.

Before leaving office the former administrator for the Local Audit and Finance section of the state treasury department opined that local government units lack legal authority to make electronic transfers of public funds. Local government officials admit that originating and receiving ACH payments is common practice, and while they believe that nothing in state law prohibits such transactions, some people would feel more comfortable if the state explicitly authorized the transactions, especially now that a treasury department official has expressed concerns. Legislation has been introduced that would authorize and regulate electronic transactions of public funds involving local units of government.

THE CONTENT OF THE BILL:

House Bill 6496 would create a new act to authorize and regulate electronic transactions of public funds involving local units of government. Specifically, the bill would allow the treasurer or the electronic transactions officer (“ETO”) of a local unit to enter into an automated clearing house (“ACH”) arrangement to originate or receive electronic payments, debits, and credit transfers processed

through an ACH. (As defined in the bill, an “electronic transactions officer” would be the person designated under the act by charter or by a local unit’s governing body. An “automated clearing house” would be defined as a national governmental organization with authority to process electronic payments, including the National Automated Clearing House Association, or “NACHA”, and the federal reserve system.)

A local unit could not be a party to an ACH arrangement unless the local unit’s governing body had adopted a resolution authorizing electronic transactions and the treasurer or the ETO of the local unit had presented a written ACH policy to the governing body. The ACH policy would have to include all of the following:

- [a statement] that an officer or employee designated by the treasurer or ETO was responsible for the local unit’s ACH agreements, including payment approval, accounting, reporting, and generally for overseeing compliance with the ACH policy;
- [a statement] that the officer or employee responsible for disbursement of funds was required to submit to the local unit documentation detailing the goods or services purchased, their cost, the date of the payment, and the department levels serviced by payment;
- a system of internal accounting controls to monitor the use of ACH transactions made by the local unit;
- the approval of ACH invoices before payment; and
- any other matters the treasurer or ETO considered necessary.

After notice and a hearing, the Department of Treasury could issue an order limiting or suspending

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the authority of a local unit to make electronic transactions under the act for failure to comply with the act's requirements or with the requirements of the local unit's ACH policy. The bill states that the act would not affect the validity of an ACH arrangement entered into by a local unit before the act's effective date, but all electronic transactions made on or after the effective date of the act would be required to comply with the act. ACH arrangements would not be subject to the Revised Municipal Finance Act or to provisions of law or charter concerning the issuance of debt by a local unit of government.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, while the bill would impose short-term costs on local units desiring to initiate electronic transactions related to developing appropriate policies and procedures under the bill, the costs would likely be offset in the long-run by savings achieved through the use of electronic transactions. (11-13-02)

ARGUMENTS:

For:

As the National Automated Clearing House Association numbers show, electronic payments are becoming increasingly popular as means of transferring funds from one individual, business, or unit of government to another. Electronic transactions are less expensive, easier to track, and more environmentally friendly than traditional paper transactions. Some people even argue that they are more secure than paper transactions; after all, checks may be lost or stolen. Many local units of government in Michigan currently authorize electronic debits and credits to their accounts. For instance, local units often allow their employees to sign up to have their paychecks deposited directly into their checking or savings accounts, and they also allow the federal government to deduct federal income taxes from the local units' payroll accounts. Those local units that do engage in electronic transactions have generally devised some set of internal control procedures to ensure the security of their transactions and the privacy of their financial information.

Although the electronic transfer of funds is a common practice among local units of government, at least one treasury department official believes that local units are on shaky legal ground. The bill would explicitly authorize local units to make electronic payments through an automated clearing house. No

less important, the bill would require a local unit wishing to engage in such transactions to adopt a policy identifying the officer who is accountable for the electronic payments and setting forth a system of internal control procedures to ensure that the payments are properly monitored. Although local units generally have their own security procedures, putting these accountability and internal control measures into state law would provide additional assurance that public funds are being handled responsibly.

Note that the bill would not require local units to engage in electronic transactions. Instead, the bill would require the governing body of a local unit to adopt a resolution authorizing the treasurer or electronic transactions officer to engage in electronic transactions. Thus, if a governing body believed that electronic transactions constituted an unacceptable risk to public funds, it could simply refuse to adopt a resolution, unless and until it was convinced otherwise.

POSITIONS:

The Michigan Municipal Finance Officers Association supports the bill. (11-13-02)

The Michigan Association of County Treasurers supports the bill. (11-13-02)

The Michigan Townships Association supports the bill. (11-13-02)

The Michigan Municipal League supports the bill. (11-13-02)

The Department of Treasury does not oppose the bill. (11-19-02)

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.