SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based only on the provisions contained in the legislation as of the latest date listed below.)

Date: April 7, 1998 Revised: ________ ________ ________ ________

Subject: State Financial Assets

	Analyst	Staff Director	Reference	Action
1.	Lombardi	Wilson	GO	Favorable/CS
2.			CJ	
3.			WM	
4.				
5.				

I. Summary:

The committee substitute creates a felony offense for causing public financial injury through culpable negligence. The offense occurs when any contract manager, entrusted by the state with the care and custody of state financial assets in a state trust fund, cause losses of the assets in excess of $100,000 over a 12-month period through culpable negligence.

The bill requires that notice of the new offense accompany every state contract in excess of $50,000.

The bill has an effective date of July 1, 1998.

II. Present Situation:

The term "contract manager" is not currently defined in the Florida Statutes. However, the state awards contracts to investment agents[1] who are entrusted with the care and custody of state financial assets. Reference is made in the statutes to professional plan administrators, for example in s. 287.057(22), F.S., and independent, nonprofit colleges and universities may be named as managers or administrators in the award of a state service contract to an agency of the state,[2] but these entities do not fulfill the same function as a "contract manager" in the context of CS/SB 2150.

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[1]Section 518.122, F.S., provides for the delegation of investment functions.

[2]See s. 287.057(21), F.S.

There is no statutory definition for exactly *what* constitutes state financial assets. However, financial assets can be liberally construed to mean monies vested and held by the state, land, buildings, equipment, and other valuable assets. Section 215.32, F.S., describes state funds[3] and requires that these funds be deposited in the State Treasury unless specifically provided otherwise. The State Treasury and the Department of Banking and Finance then account for the funds and disburse them among the three types of state funds: the General Revenue Fund, trust funds[4], and Working Capital Fund.

State trust funds earmark funds for a specific purpose and objective and establish specific projects and programs in conjunction with the appropriation. Governmental agencies cannot always manage these projects and programs in whole or part either because they do not possess the internal resources to manage the project or program or they do not possess the necessary systems and expertise to support the task at hand. Consequently, the state may look outside to companies or entities that possess the necessary expertise to manage the project or program more efficiently and cost effectively. Hence, they transfer the duties and responsibilities to the entity on behalf of the state in a fiduciary[5] capacity. These companies or entities could also be classified as program administrators or more applicable here “contract managers.”

The Auditor General, under the provisions of s. 11.45, F.S., has the authority to conduct performance audits, and periodically monitor and review programs, activities, and functions of these contract managers. However, although a deterrent, it does not preclude an individual who has access to monetary resources from misdirecting funds. Although specific sanctions may exist for theft[6], embezzlement, or conspiracy[7], no statute sanctions poor performance.

Many public officers are required to furnish a bond that insures the faithful performance of their respective duties, particularly in cases in which duties of the office pertain to the oversight of public monies or other assets, or the safety and protection of citizens. To this end, the State Treasurer is required[8] to give a bond in the amount of $100,000; the Comptroller is required[9] to

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[3]Revenue, including licenses, fees collected or received under the authority of the laws of the state by each and every state official, office, employee, bureau, division, board, commission, institution, agency, or undertaking of the state or the judicial branch.

[4]Section 19(f), Art. III, Florida Constitution, states that no trust fund may be created by the state or other public body without a three-fifths vote of the membership of each house of the legislature. Section 215.3207, F.S., provides that each trust fund must be created by statutory language that specifies: the name of the trust fund, the agency or branch of state government responsible for administering the trust fund, the requirements or purpose that the trust fund is established to meet, and the sources of moneys to be credited to the trust fund or specific sources of receipts to be deposited in the trust fund.

[5]Section 518.14, F.S., defines “fiduciary” as an executor, administrator, trustee, guardian, or other person, whether individual or corporate, who by reason of written agreement, will, court order, or other instrument has the responsibility for the acquisition, investment, reinvestment, exchange, retention, sale, or management of money or property of another.

[6]Section 812.014, F.S.

[7]Section 777.04, F.S.

[8]Section 18.01, F.S.

[9]Section 17.01, F.S.

give a bond in the amount of $50,000; and the Commissioner of Agriculture is required[10] to give bond in the amount of $10,000. In addition, the Division of Purchasing of the Department of Management Services purchases a blanket faithful performance of duty bond that includes state employees and public officials.

On a case by case basis, the State Board of Administration contractually imposes on its external investment managers fidelity bonding requirements to indemnify the state from potential losses. The bonding requirements encompass both real estate transactions and investment securities transactions and can range from $1-$2 million.

III. Effect of Proposed Changes:

Section 1. The committee substitute defines "contract manager" to mean any person who has been given the custody, and awarded the privilege, of administering state financial assets in state trust funds pursuant to a contract. The bill also specifically captures businesses and any of its owners, operators, officers, directors, or partners or other individuals engaged in the *day-to-day* management activities of the business.

The term "entrusted by the state" is defined to mean that the state has given custody of and disbursement authority over state financial assets to the contract manager by means of a contract, without regard to whether there exists a fiduciary relationship between the state and the contract manager. Further, "state financial assets," as created in the context of this law, specifically means monetary funds intended for, existing in, or owed to any state trust fund, *not invested or held by or on behalf of the State Treasurer or the State Board of Administration*, and includes any negotiable or other monetary instrument drawn on or disbursed from a trust fund.

Section 287.133, F.S., prohibits persons convicted of crimes against a public entity from conducting business transactions with state government.[11] Senate Bill 2150, by specifically capturing businesses and business owners, operators, officers, directors, partners, or other individuals engaged in the management activities of the business as contract manager is not a significant departure from those historically considered influential in committing public entity crimes.

"[C]ulpable negligence" is defined to mean negligence of a gross and flagrant character which evinces a reckless disregard for the state financial assets entrusted to a contract manager and leads to a presumption of indifference to the consequences.

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[10]Section 19.14, F.S.

[11]Section 287.133, F.S., denies the right to those already convicted of a public entity crime to transact business with public entities. Those denied the right of conducting business transactions include: a predecessor or successor of a person convicted of a public entity crime; an entity controlled by a person who also actively manages and has been convicted of a public entity crime not to the exclusion of officers, directors, executives, partners, shareholders, employees, members, and agents; ownership by one person constituting a controlling interest in another person; or a person who knowingly enters into a joint venture with another who has been convicted of a public entity crime during the preceding 36 months.

Section 2. A felony is created with four elements which must be proved for conviction. The elements include: the person must be a "contract manager," the person must be entrusted by the state with the care and custody of state financial assets in a state trust fund; the person causes loss, or through inactions, causes loss of state assets in excess of $100,000 over a 12-month period; and the person causing the loss does so by being culpably negligent.

A felony is created and is punishable in the third degree. In this context, a third degree felony is punishable by not more than 5 years in prison and a $5,000 fine for losses valued at $100,000 or more, but less than $250,000. Section 775.083(1)(f), F.S., also provides for a higher amount equal to double the pecuniary gain derived from the offense by the offender or double the pecuniary loss suffered by the victim. The state attorney or the Statewide Prosecutor reserves the right to prosecute on behalf of the state for violations of this act.

The bill requires that notice of the new offense accompany every state contract in excess of $50,000.

Section 3. The act shall take effect July 1, 1998.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

In implementing the provisions of s. 8.(d), Art. II, State Constitution, it is the Legislature's intent to sanction those public officers or employees:[12] committing, aiding, or abetting of an embezzlement of public funds; or committing, aiding, or abetting of any theft of funds of an employer; bribery in connection with employment; committing an impeachable offence; or who willfully and with intent to defraud the public or the public agency from which the public officer or employee acts.

[12]Section 112.3173(1)(c), F.S., defines public officer or employee to mean an officer or employee of any public body, political subdivision, or public instrumentality within the state.

The state shall hold liable for damages any public officer or employee who breaches the public trust for private gain or any person or entity inducing a breach. In addition, any public officer or employee who is convicted of a felony involving a breach of public trust will be subject to forfeiture of right and privileges under a public retirement system or pension plan in such manner as may be provided by law.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

According to the four elements of felony in the bill, the "contract manager" does not have to cause the loss of state assets directly. Felony charges may also be brought upon a contract manager, who, through inaction, allows financial losses in the aggregate valued at $100,000 or more. The inclusion of the word "inaction" extends to directors, shareholders, partners, or other individuals not directly engaged in day-to-day operations or management activities but the review thereof. Through position or affiliation, these individuals could be charged for "not acting", thus allowing public financial injury. If information by an internal manager(s) with intent to defraud or commit fraud, is not fully disclosed, then directors, shareholders, partners, or other individuals who are one removed from the normal day-to-day operations of the business may gain knowledge of the felony after the fact.

VII. Related Issues:

The Statewide Prosecutor has provided the following examples of instances where the bill would make criminal prosecution possible:

Example 1. Business A contracted to administer a state trust fund. However, due to inexperience and/or incompetence, such as a failure to exercise care in hiring personnel, the business was unable to meet its contractual obligations. Furthermore, without the knowledge of high ranking corporate officials, low level employees attempted to steal the fund's assets. Losses to the trust fund had to be replaced at cost to the taxpayer. Although it was clear that business A

had no prior experience administering this type of trust fund, there is no proof that business A fraudulently intended to enter into the contract.

Example 2. Business B contracted with a state agency to administer state trust fund #2. Business B took no steps to safeguard the handwritten checkbook, but left it unsecured where several low-level employees had access. The checks did not require two signatures; nor did the checks require access to a check-writing machine. Although the managerial employees were responsible for the security of the company and standard security measures were not followed, there was no proof that the managerial employees conspired with the low-level employees to steal the state's money.

An impetus for this bill stems from an ongoing investigation being undertaken by the Statewide Prosecutor of the circumstances under which the State of Florida contracted the management of its state employee health insurance program to a third party administrator, Unisys, Incorporated. In the course of the contract, cumulative recurring and nonrecurring losses exceeding $300 million were experienced. Testimony from the Division of State Group Insurance has attributed these losses to the inability of the third party administrator to perform its duties under terms of the contract, its inability to received the represented discounts from providers, as well as the suppression of premium increases by the State for the prior five years. The company has paid several million dollars in liquidated damages for its performance shortcomings. In mid-1997 Unisys entered into an agreement in which it terminated its active management of the plan effective January 1, 1998. Blue Cross and Blue Shield of Florida was designated the successor third party administrator for the plan.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.