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****AS PASSED BY THE LEGISLATURE****
CHAPTER #: 2001-230, Laws of Florida

HOUSE OF REPRESENTATIVES

STATE ADMINISTRATION FINAL ANALYSIS

BILL #: HB 625, 1st ENG
RELATING TO: Security for Public Deposits
SPONSOR(S): Representative(s) Bean and others
TIED BILL(S): None

ORIGINATING COMMITTEE(S)/COUNCIL(S)/COMMITTEE(S) OF REFERENCE:

- (1) STATE ADMINISTRATION YEAS 5 NAYS 0
- (2) BANKING YEAS 7 NAYS 0
- (3) COUNCIL FOR SMARTER GOVERNMENT YEAS 11 NAYS 0
- (4)
- (5)

I. SUMMARY:

On June 13, 2001, HB 625, 1st Engrossed was approved by the Governor and became law as Chapter 2001-230, Laws of Florida (the "act"). The effective date of the act is October 1, 2001.

The Cabinet office of the Treasurer was established under the State Constitution. The Treasurer is responsible for keeping all state funds and securities and investing excess funds in qualified public depositories. The Treasurer is also responsible for establishing qualifications in order to designate banks and savings and loan associations as qualified public depositories. A qualified public depository is required to collateralize a specified portion of the public monies on deposit so that the designated portion of the public deposits is immediately available should the need arise.

This act eliminates the advisory committee to the qualified public deposit program and establishes the Qualified Public Depository Oversight Board (Oversight Board) comprised of six members and six alternate members. The Oversight Board represents the interests of all qualified public depositories in safeguarding the integrity of the program and preventing the realization of loss assessments. The Treasurer selects two members that represent public depositories in each of the three asset groups.

This act authorizes the use of Federal Home Loan Bank letters of credit as eligible collateral, when certain requirements are met.

This act also requires a qualified public depository to pledge, deposit, or issue additional eligible collateral between filing periods of monthly reports, within two business days, when notified by the Treasurer that the current market value of the collateral does not meet the collateral requirements. A qualified public depository is prohibited from acting as its own custodian.

Violations subject to administrative penalties are revised to include failure to maintain required collateral rather than failure to pledge sufficient collateral and the Treasurer is authorized to issue a cease and desist order if a qualified public depository deposits or arranges for the issuance of unacceptable collateral.

This act does not appear to have a fiscal impact on state or local governments.

II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

- | | | | |
|-----------------------------------|------------------------------|-----------------------------|-----------------------------------------|
| 1. <u>Less Government</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 2. <u>Lower Taxes</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. <u>Individual Freedom</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 4. <u>Personal Responsibility</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 5. <u>Family Empowerment</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |

For any principle that received a "no" above, please explain:

B. PRESENT SITUATION:

Office of the Treasurer

The Cabinet office of the Treasurer was established in s. 4, Art. IV, Florida Constitution. The Treasurer is directed to keep all state funds and securities and to disburse state monies only upon the order of the Comptroller. The Treasurer administers the Government Employees Deferred Compensation Plan through the Division of the Treasury.¹

The Treasurer is required to invest monies in excess of those needed to pay the immediate debts of the state. These excess funds include monies from the General Revenue Fund, trust accounts, and various other accounts of state agencies and other public and quasi-public entities. The law authorizes the Treasurer to charge a fee for managing excess state monies.²

Pursuant to s. 18.10(2), F.S., the Treasurer is directed to invest these excess funds in qualified public depositories that will pay rates established by the Treasurer at levels not less than the prevailing rate for United States Treasury securities with a corresponding maturity. In the event additional money is available and qualified public depositories are unwilling to accept such money and pay the rates established by the Treasurer, then the Treasurer is authorized to invest the money in specific investment products.³

The law also directs that the Treasurer establish qualifications in order to designate banks and savings and loan associations as qualified public depositories.⁴ Chapter 280, F.S., outlines the procedures a financial institution must follow in order to be designated as a qualified public depository.

Qualified Public Depository

In order to qualify as a qualified public depository, a financial institution must provide specific information to the Department of Insurance describing the assets of the institution. A qualified public depository is also required to collateralize a specified portion of the public monies on deposit

¹ See s. 20.13(6)(a), F.S.

² See s. 18.103(2), F.S.

³ See s. 18.10(2), F.S.

⁴ See s. 280.05, F.S.

so that the designated portion of the public deposits is immediately available should the need arise. The percentage of public funds that a financial institution must collateralize varies depending upon the assets of the institution and other factors.⁵

Federal Reserve Banks

Effective January 1, 1997, the Federal Department of Treasury established new regulations governing book-entry securities for Federal Reserve Banks. These regulations changed the procedures relative to acting as custodians of the Treasury and agency book-entry securities pledged as collateral for state and local deposits or in conjunction with the exercise of trust powers. These changes required the Treasurer to enter into custody agreements with the Federal Reserve Banks using their form that included unacceptable provisions, for example, liability for the state and waiver of sovereign rights. The Federal Reserve Banks are not subject to the provisions of the Uniform Commercial Code. In the past, the federal Treasury had signed the forms prescribed by the Treasurer. As of January 2, 1998, a Federal Reserve Bank no longer acts as a custodian pursuant to these agreements and safekeeping receipts previously executed. Since that time, the Treasurer's Office has been in negotiations with the Federal Reserve Banks.⁶

C. EFFECT OF PROPOSED CHANGES:

Section 280.02, F.S.

This act amends s. 280.02, F.S., to revise and add definitions.

- “Alternative participation agreement,” is defined to mean an agreement to restrictions which a qualified public depository must complete as an alternative to immediately withdrawing from the public deposits program due to financial condition.
- “Eligible collateral,” is expanded to include Federal Home Loan Bank letters of credit and cash.
- “Market value” is defined to mean the value of collateral calculated pursuant to s. 280.04, F.S.
- “Oversight board” is defined to mean the Qualified Public Depository Board⁷ for the purpose of safeguarding the integrity of the public deposits program and preventing the realization of loss assessments through standards, policies, and recommendations for action made to the Treasurer.
- “Public deposit program,” is revised to mean the Florida Security for Public Deposits Act and any rules adopted under chapter 280, F.S.
- The definition of “triggering events” is amended such that if a “triggering event” occurs, the Treasurer is authorized to demand payment under letters of credit.

⁵ See s. 280.04, F.S.

⁶ See Senate Staff Analysis and Economic Impact Statement by the Committee on Banking and Insurance, March 26, 2001.

⁷ The Qualified Public Depository Board was created pursuant to s. 280.071, F.S.

Section 280.04, F.S.

This act amends s. 280.04, F.S., relating to collateral for public deposits. It revises the collateral deposit requirements for a qualified public depository to require collateral as required in special instructions from the Treasurer. The deadline for a qualified public depository to meet additional collateral requirements is two business days instead of 48 hours.

In addition, each qualified public depository must value its collateral by using 100 percent of the maximum amount available, under the Federal Home Loan Bank letters of credit, as market value. Each qualified public depository is also required to report its required collateral on the monthly report required pursuant to s. 280.16, F.S., and must simultaneously pledge, deposit, or issue eligible collateral as needed.

Each qualified public depository is required to report to the Treasurer any material declines in value, that occur prior to the date of the submission of the monthly report that is required, pursuant to s. 280.16, F.S.

A qualified public depository must pledge, deposit, or issue additional eligible collateral between filing periods of the monthly report, when notified by the Treasurer that the current market value of the collateral did not meet the collateral requirements. This additional collateral is required within two business days after the Treasurer's notification. In the event that a qualified public depository fails to meet the collateral requirements, it could be required to return public deposits to governmental units and be suspended, disqualified, or subjected to administrative penalty.⁸

The Treasurer must adopt rules for the establishment of collateral requirements, collateral pledging levels, required collateral calculations, and market value, and clarifying terms.

Section 280.041, F.S.

This act amends s. 280.041, F.S., to establish collateral arrangements that can be used by a qualified public depository or an operating subsidiary to meet collateral requirements. The regular custody arrangement requires the pledging of the collateral with a custodian. Federal Home Loan Bank letters of credit arrangements are authorized as eligible collateral and requirements are established for such collateral.

A qualified public depository is prohibited from acting as its own custodian. If the custodian fails to meet certain reporting or records requests, then the qualified public depository is prohibited from using the custodian for a one-year period.

This act provides that if there is any change in the Uniform Commercial Code, which affects the requirements for a perfected security interest in collateral, the Treasurer must notify the custodian of such collateral regarding such change.

The Federal Reserve Bank custody arrangement requires the pledging of collateral to the Treasurer. However, the Federal Reserve Bank agreement cannot subject the Treasurer to any costs or indemnification requirements.

The Treasurer's custody arrangement requires collateral to be deposited in the Treasurer's name. The collateral is then held in a custodial account established in the Treasurer's name as a designated custodian.

⁸ The administrative penalty is provided in ss. 280.051 and 280.054, F.S.

The Federal Home Loan Bank letter of credit arrangement requires that the collateral be issued with the Treasurer as the beneficiary. A completed agreement containing the following provisions is necessary:

- The letter of credit must meet the definition of eligible collateral;
- The Treasurer, as beneficiary, can, without notice to or consent by the qualified public depository, demand payment under the letter of credit if any of the triggering events⁹ occur;
- Funds received by the Treasurer due to the occurrence of one or more triggering events can be deposited in the Treasury Cash Deposit Trust Fund for purposes of eligible collateral;
- The qualified public depository must arrange for the issue of letters of credit¹⁰ and delivery to the Treasurer;
- The qualified public depository is responsible for all costs necessary to use or confirm the letters of credit issued on behalf of the Treasurer;
- In the event of litigation, the qualified public depository must be subject to jurisdiction of the courts of this state or the courts of the United States;
- Any information, form, or report electronically transmitted to the Treasurer must have the same enforceability as a signed writing;
- The qualified public depository must submit proof that authorized individuals executed the letters of credit on the depository's behalf; and
- The qualified public depository must agree, by resolution of its board of directors, that these letters of credit have been formally accepted and constitute official records of the depository.

The triggering events authorizing the Treasurer to demand payment, under a letter of credit, or direct a custodian to deposit or transfer collateral and proceeds are expanded to include when:

- The Federal Home Loan Board or the qualified public depository gives notice that a letter of credit will not be extended or renewed and other eligible collateral has not be deposited; and

⁹ Section 280.02(28), F.S., defines "triggering events" as "events set out in subsection 280.041(4) which give the Treasurer, as pledgee, the right to instruct the custodian to transfer securities pledged, interest payments, and other proceeds of pledged collateral not previously credited to the pledgor." These events include when: the Treasurer determines that an immediate danger to the public health, safety, or welfare exists; the qualified public depository defaults or becomes insolvent; the qualified public depository fails to pay an assessment; the qualified public depository fails to pay an administrative penalty; and the qualified public depository fails to meet financial condition standards. (Section 280.041(4), F.S.)

¹⁰ The letters of credit must meet the requirements of s. 280.13, F.S.

- The depository, if involved in a merger, acquisition, consolidation, or other organizational change, fails to notify the Treasurer or ensure that required collateral is properly maintained by the depository holding the Florida public deposits.

Section 280.05, F.S.

This act amends s. 280.05, F.S., to eliminate the advisory committee and to create the Qualified Public Depository Oversight Board (Oversight Board).

The Treasurer is required to identify representative qualified public depositories and to furnish notification for the selection of the Oversight Board. The Treasurer is also required to provide certain data to the Oversight Board to assist the Oversight Board in establishing standards for qualified public depositories and custodians, to evaluate requests for exceptions to standards and alternative participation agreements, and review and recommend action concerning a violation committed by a qualified public depository. The Treasurer can review, implement, monitor, evaluate, and modify all or any part of the standards, policies, or recommendations of the Oversight Board.

The Treasurer is authorized to issue notice to a qualified public depository that the use of a custodian is not allowed if the custodian has failed to follow the terms of a collateral agreement. The Treasurer can demand payment, under letters of credit, for any triggering events listed in s. 280.041, F.S., and deposit the funds into the Public Deposits Trust Fund for purposes of paying losses to public depositors. The Treasurer is authorized to deposit administrative penalties into the Treasurer's Administration and Investment Trust Fund and to deposit eligible collateral into the Treasury Cash Deposit Trust Fund.

Section 280.051, F.S.

This act amends s. 280.051, F.S., to revise the grounds for suspending or disqualifying a qualified public depository to include failure to maintain required collateral, rather than failure to pledge sufficient collateral, to cover public deposits.

Section 280.054, F.S.

This act amends s. 280.054, F.S., to revise the grounds for administrative penalties and disqualification to include failure to provide required collateral using eligible collateral and prescribed collateral agreements, or withdrawing collateral without the Treasurer's approval. A qualified public depository is subject to an administrative penalty in an amount not to exceed the greater of \$1,000 or 10 percent of the amount of withdrawal, not exceeding \$10,000 for either of these violations.

Section 280.055, F.S.

This act amends s. 280.055, F.S., to clarify that the Treasurer can issue a cease and desist order and a corrective order upon determining that a qualified public depository deposits, or arranges for the issuance of, unacceptable collateral, in addition to "pledging" as provided in current law.

Section 280.07, F.S.

This act amends s. 280.07, F.S., to change the title of the section from "Mutual Responsibility" to "Mutual Responsibility and Contingent Liability," in order to more clearly reflect the provisions of this

section. This act provides that any entity designated as a qualified public depository, which is not insolvent, is required to guarantee public depositors against loss caused by the default of insolvency of other qualified public depositories.

Section 280.071, F.S.

This act creates s. 280.071, F.S., to establish the Oversight Board. The Oversight Board consists of six members and six alternate members who represent the interests of the qualified public depositories in safeguarding the integrity of the program and preventing the realization of loss assessments.

On July 31 of each year, and as vacancies occur, the Treasurer must initiate the selection of the Oversight Board representation by

- Categorizing eligible qualified public depositories¹¹ into three groups according to average asset size;
- Identifying the two qualified public depositories in each of the three asset groups that have the greatest shares of contingent liabilities; and
- Sending notification to the six qualified public depositories that have been identified.

Each of the six representatives must select a member and an alternate member of the Oversight Board, and notify the Treasurer of the selection within 30 days after the Treasurer's notification. If the qualified public depository selected by the Treasurer declines to participate, the Florida Bankers Association must select a member and an alternate member within 30 days to represent the average asset category. The Oversight Board members and alternate Oversight Board members are subject to the approval of the Treasurer. The alternate member must serve in the event that the Oversight Board member is unable to perform his or her duties. Each Oversight Board member must serve until a successor is selected.

The duties of the members of the Oversight Board include:

- Having resources available for review of qualified public depository issues; and
- Possessing knowledge and experience in financial analysis, accounting, banking, risk management, or investment management.

A qualified public depository must pay for its Oversight Board member's expenses, incurred by that member in carrying out his or her duties.

Policies and procedures for organizing, communicating, and conducting Oversight Board meetings are prescribed. In the absence of a quorum, the Treasurer or his or her representative must vote as a member.

¹¹ An "eligible qualified public depository" is defined to mean a qualified public depository that is "in compliance with all requirements and shall not be suspended, disqualified, or withdrawing, or under an alternative participation agreement in the public deposits program." (Section 9 of HB 625, 1st Engrossed)

The Oversight Board is charged with establishing standards for reporting requirements, custodian characteristic requirements and adherence to collateral agreement terms, collateral eligibility and restrictions, conditions for suspension and disqualification, penalties and fines, and corrective actions and administrative orders. The Oversight Board is also responsible for recommending to the Treasurer the approval or rejection of requests for exceptions that do not meet established standards. The Oversight Board must approve or reject alternative participation agreements referred by the Treasurer. The Oversight Board is also responsible for reviewing program violations and recommending that the Treasurer impose penalties and fines or issue corrective actions and administrative orders. The Oversight Board is also authorized to assess qualified public depositories for the implementation of standards established by the Oversight Board, which exceed the funding of the program.

All official actions of the Oversight Board regarding the establishment of standards, decisions regarding exceptions and alternative participation agreements, and recommendations concerning violations must be communicated to the Treasurer in writing and are subject to the approval of the Treasurer.

The Treasurer is authorized to adopt rules establishing forms and procedures for the selection of members and alternate members of the Oversight Board, and governing functions.

Section 280.08, F.S.

This act amends s. 280.08, F.S., to revise procedures for determining the loss to public depositors in the event that a default or insolvency occurs, to incorporate the use of letters of credit. The loss to any public depositor continues to be satisfied first through any applicable deposit insurance, and then through demanding payment under letters of credit or the sale of collateral, instead of securities, pledged.

Section 280.09, F.S.

This act amends s. 280.09, F.S., relating to the Public Deposits Trust Fund. It incorporates the acceptance of letters of credit and allows for the draw on letters of credit held as collateral. A cross-reference is updated.

Section 280.10, F.S.

This act amends s. 280.10, F.S., to clarify the current provisions which provide that the public deposits and associated collateral of a qualified public depository that is merged with, acquired by, or consolidated with another financial institution, are public deposits of the resulting institution. If the resulting institution does not want to participate in the public deposits program, it must provide written notice of intent to withdraw and a proposed effective date of withdrawal. The proposed effective date must be 180 days after the effective date of the acquisition, merger, or consolidation. The Treasurer must initiate a mandatory withdrawal of the resulting institution, if the resulting institution does not provide certain documents or does not meet the program requirements. Procedures for the disposition of Florida public deposits or collateral are provided.

Section 280.11, F.S.

This act amends s. 280.11, F.S., to correct a cross-reference.

Section 280.13, F.S.

This act amends s. 280.13, F.S., to include letters of credit issued by the Federal Home Loan Bank as eligible collateral if certain conditions are met, including the delivery of the letter of credit to the Treasurer and designating the Treasurer as the beneficiary.

Section 280.16, F.S.

This act amends s. 280.16, F.S., to require the collateral control agreements and letters of credit to be made under oath.

D. SECTION-BY-SECTION ANALYSIS:

See "Effect of Proposed Changes."

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Section 280.071, F.S., Qualified Public Depository Oversight Board, may be an expense to banks and savings associations in the following ways:

- Oversight Board members will be using resources in the review of qualified public depository issues. These resources are the members' time, electronic communication methods, express delivery services, and research tools.
- The representative depositories pay for the expenses of oversight board members, in carrying out duties of the board. These expenses include travel and meeting expenses.

- Assessing the qualified public depositories participating in the program may pay standards implemented by the Oversight Board, which exceed the resources of the public deposits program.¹²

This section also allows the banks and savings associations that have the greatest contingent liabilities in the program to have the greatest impact on the program standards, exceptions, and violations. These areas influence the potential for the realization of assessments.¹³

Section 280.13, F.S., Eligible Collateral, adds Federal Home Loan Bank letters of credit as a collateral type. Using this collateral type will cost the banks and savings associations a fee. In addition, using this collateral type allows the banks and savings associations to select a collateral type that will not affect regulatory liquidity calculations.¹⁴

D. FISCAL COMMENTS:

This act relates to the management of the public depository program administered by the State Treasurer. Provisions of this act may have an indirect effect on the Financial Institutions Regulatory Program by allowing or restricting financial institution participation as qualified public depositories. However, the Department of Banking & Finance does not believe that the ability or inability to be a qualified public depository will have an impact on the viability of any financial institution, and, as such, this act does not appear to have a fiscal impact on the Financial Institutions Regulatory Program.¹⁵

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This act does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This act does not reduce the authority that municipalities or counties have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This act does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

None.

¹² See Senate Staff Analysis and Economic Impact Statement by the Committee on Banking and Insurance, March 26, 2001.

¹³ *Id.*

¹⁴ *Id.*

¹⁵ Fiscal Note for HB 625 from the Department of Banking & Finance, March 15, 2001.

B. RULE-MAKING AUTHORITY:

This act authorizes the Treasurer to adopt rules for “the establishment of collateral requirements, collateral pledging levels, required collateral calculations, and market value and clarifying terms.”

C. OTHER COMMENTS:

None.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On March 29, 2001, the Committee on State Administration adopted a strike-everything amendment to HB 625. The strike-everything amendment makes a number of technical and editorial changes; eliminates a public records exemption that was inadvertently included in the bill; adds a needed cross-reference; and provides that if there is any change in the Uniform Commercial Code, which affects the requirements for a perfected security interest in collateral, the Treasurer must notify the custodian of such collateral regarding such change.

The committee reported out HB 625 favorably with one amendment. This strike-everything amendment is traveling with the bill.

VII. SIGNATURES:

COMMITTEE ON STATE ADMINISTRATION:

Prepared by:

Heather A. Williamson, M.S.W.

Staff Director:

J. Marleen Ahearn, Ph.D., J.D.

AS REVISED BY THE COMMITTEE ON BANKING:

Prepared by:

Michael A. Kliner

Staff Director:

Susan F. Cutchins

AS FURTHER REVISED BY THE COUNCIL FOR SMARTER GOVERNMENT:

Prepared by:

Heather Williamson, M.S.W.

Staff Director:

Don Rubottom

FINAL ANALYSIS PREPARED BY THE COMMITTEE ON STATE ADMINISTRATION:

Prepared by:

Heather A. Williamson, M.S.W.

Staff Director:

J. Marleen Ahearn, Ph.D., J.D.