STORAGE NAME: h1831a.in
DATE: March 29, 2000

HOUSE OF REPRESENTATIVES
COMMITTEE ON
INSURANCE
ANALYSIS

BILL #: HB 1831

RELATING TO: Public Deposits

SPONSOR(S): Representative Trovillion

TIED BILL(S):

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

(1) INSURANCE YEAS 16 NAYS 0
(2) FINANCIAL SERVICES
(3) GOVERNMENTAL RULES & REGULATIONS
(4) GENERAL GOVERNMENT APPROPRIATIONS
(5)

I. SUMMARY:

The Florida Security for Public Deposits Act (the Act) was enacted in 1981. The Act outlines the procedures a financial institution must follow in order to be designated as a qualified public depository. The Treasurer is charged with administering the Act, which protects the accounts of public depositors in the event of a default or insolvency of a bank or savings association that operates as a public depository.

HB 1831 would make a number of changes to the Act, including:

- ♦ establishing a new requirement to allow a bank to remain a qualified public depository by maintaining minimum required collateral of $100,000. Other requirements regarding pledging levels and the required collateral would remain the same, but the language would be restated for clarification purposes and rules promulgated by the Treasurer would be codified.

- ♦ revising the Act to set forth the nature of the collateral agreements between the pledgor, the custodian, and the Treasurer. These changes would allow the Treasurer to have a perfected security interest in the event that the Treasurer needed to take control of the collateral.

- ♦ identifying triggering events in which the Treasurer could require the deposit or transfer of collateral into a custodial account established for the Treasurer.

- ♦ eliminating Federal Home Loan time deposits and negotiable certificates of deposits as acceptable collateral types.

This bill would not have an impact on state or local government.

Amendments

On March 28, 2000, the Committee on Insurance adopted a “strike everything” amendment which is traveling with the bill. For an explanation, refer to the Amendment section of the analysis.

II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

1.	Less Government	Yes []	No []	N/A [x]
2.	Lower Taxes	Yes []	No []	N/A [x]
3.	Individual Freedom	Yes []	No []	N/A [x]
4.	Personal Responsibility	Yes []	No []	N/A [x]
5.	Family Empowerment	Yes []	No []	N/A [x]

B. PRESENT SITUATION:

Florida Security for Public Deposits Act
Under Article IV, Section 3 of the Florida Constitution, the Treasurer is charged with keeping all state funds and securities and dispersing these funds upon the order of the Comptroller. Section 18.10, Florida Statutes, requires the Treasurer to deposit funds in the Treasury in "qualified public depositories" that offer collateral security for the funds deposited.

The Legislature enacted the Florida Security for Public Deposits Act (the Act) in 1981. The Act outlines the procedures a financial institution must follow in order to be designated as a qualified public depository. The Treasurer is charged with administering the act, which protects time deposits and checking accounts of public depositors (the state, any county, school district, community college district, special district, metropolitan government, municipality, or court) in the event of a default or insolvency of a bank or savings association that operates as a public depository.

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 so that the public deposits are available immediately should the need arise.

The Act sets forth percentages of public funds that a qualified public depository must collateralize. That amount varies depending upon the assets of the institution and other factors. The pledging levels that qualified public depositories must meet and the collateral requirements are set forth in the Act and Rules 4C-2.006 and 4C-2.024, Florida Administrative Code.

The collateral pledged by a qualified public depository is kept by a custodian, which is a bank, trust company or savings association that has met certain requirements and is approved by the Treasurer. The three parties involved, the Treasurer, the pledgor (i.e., the qualified public depository), and the custodian must enter into a "public depository pledge agreement," the details of which are set forth in the Act and in Rule 4C-2, Florida Administrative Code.

The Act and Rule 4C-2.006, Florida Administrative Code, also set forth the treatment of the transfer, withdrawal, and substitution of collateral (i.e., collateral transactions).

According to the annual report of the Treasurer, as of June 30,1999, there were 205 qualified public depositories. The total average daily balance of public deposits for June 1999, was approximately $4.5 billion, and the reported market share of pledged collateral was almost $3 billion.

Uniform Commercial Code (UCC)
The Uniform Commercial Code (UCC) consists of eleven articles and was created to promote uniformity among the states in all phases of a commercial transaction to facilitate interstate trade.

The Legislature amended Chapters 678 and 679, Florida Statutes, effective October 1, 1998, to adopt a previously unaddressed, yet fully functional, system of securities holdings: one that uses securities intermediaries, such as broker-dealers, that hold the actual security certificates on behalf of the certificate owners. The changes also reflected the increased use of electronic technology for the transfer of securities where the securities owner does not have physical possession of the security certificate.

Chapter 678, F.S., provides for the perfection of a security interest in an investment property. Perfection of a security interest deals with the steps legally required to give a secured party an interest in the property against the debtor's creditors. Chapter 679, F.S., sets forth the rights of third parties and the rules of priority regarding perfected and unperfected security interests.

Perfection of security interests can occur in one of at least two ways: by control or by filing. "Perfection by control" means that the secured party has taken whatever steps are necessary to place itself in a position where it can have securities sold, without further action by the owner. The method by which a secured party perfects by control depends upon the nature of the collateral. For example, in the case of certificated securities, control is simply the delivery of possession of the certificate, with applicable endorsement. For a security interest in an uncertificated security, the secured party may perfect control by becoming registered with the issuer as the holder of the uncertificated securities or by the issuer, pledgor, and the secured party executing a control agreement that includes provisions whereby the issuer agrees that it will comply with instructions originated by the secured party without further consent by the pledgor. It must be clear that the secured party has the right to liquidate the collateral without the consent of or any action by the pledgor.

"Perfection by filing" provides that perfection may be obtained by execution of a security agreement between the pledgor and the secured party containing language that clearly creates a security interest or by filing a financing statement covering the collateral described in the security agreement.

Perfection by control and by filing protect the secured party against liens asserted by third parties, but the secured party who perfects its interest by obtaining control has priority.

Federal Reserve Banks As Custodian for Public Depositories
Effective January 1, 1997, the Federal Department of the Treasury established new regulations governing those securities that are not represented by paper certificate, but rather by an account entry (i.e., book-entry securities) for Federal Reserve Banks. This changed the procedures relative to Federal Reserve Banks acting as custodians of the state 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 state Treasurer to enter into custody agreements with the Federal Reserve Banks using their form that included 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 state 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.

Certificates of Deposits Purchased by Insurers
Insurance companies are required under Florida law to purchase certificates of deposit from qualified public depositories. Insurance companies may perceive these funds to be protected against loss in the event of a depository becoming insolvent or in default. However, the Florida Security for Public Deposit Act protects only public deposits.

C. EFFECT OF PROPOSED CHANGES:

HB 1831 would make a number of changes to the Florida Security for Public Deposits Act. Section 280.02, Florida Statutes, would be amended to define certain terms used in the Florida Security for Public Deposits Act.

Section 280.04, Florida Statutes, regarding collateral for public deposits, would be reworded. While the general provisions for determining the collateral requirements and the pledging levels of qualified public depositories would remain the same, a new requirement would be established to allow a bank to remain a qualified public depository by maintaining minimum required collateral of $100,000. This would allow banks that are established qualified public depositories, but are not currently holding public deposits to remain qualified public depositories so they could be prepared to collateralize public deposits within 48 hours without having to re-qualify as a public depository.

Additionally, a bank that has a low quarterly financial ranking and does not want to withdraw as a public depository would be required to pledge collateral equal to 200 percent of the amount of public deposits it holds for the Treasurer. The Treasurer currently requires banks to do this by Rule 4C-2.024, Florida Administrative Code.

Section 280.041, F.S. would be created to set forth the nature of the collateral agreements between the pledgor, the custodian, and the Treasurer. These changes would allow the Treasurer to perfect the collateral in the event that the Treasurer needed to take control of the collateral.

The requirement that the certificates of deposit which are purchased by insurers and insurance agents and required to be deposited with the DOI as part of the insurer's or agent's authority to transact business in the state be purchased from a qualified public depository would be eliminated. This requirement would offer no protections under Chapter 280, Florida Statutes.

The requirement that all trust institutions pledge security would be eliminated. Trust companies would continue to be required to pledge security. The responsibility for administering collateral requirements would be transferred from the Treasurer to the Department of Banking and Finance.

D. SECTION-BY-SECTION ANALYSIS:

Section 1 amends s. 280.02, F.S., to define a number of terms relating to public deposits, including affiliate, book-entry form, operating subsidiary, pledged collateral, pledgor, pool figure, Treasurer's custody, and triggering event. Additionally, the terms “collateral-pledging level” and “public deposit” would be amended.

Section 2 rewords and makes technical changes to s. 280.04, F.S., relating to the collateral levels required by the Treasurer for a qualified public depository.

Section 3 creates s. 280.041, F.S., relating to collateral arrangements, agreements, provisions, and triggering events.

A qualified public depositor would be allowed to deposit collateral with a custodian and would be required to submit a collateral agreement for approval by the Treasurer.

As part of the collateral agreement, the pledgor would agree: to own the pledged collateral; to grant the Treasurer an interest in the collateral and not enter into or execute another agreement related to the collateral without the written consent of the Treasurer; not to grant the custodian a lien that attaches to the collateral in favor of the custodian that is superior or equal to the interest of the Treasurer; that the Treasurer could require the custodian to comply with and perform all requests and orders from the Treasurer, including liquidating the collateral or transferring the collateral directly to the Treasurer; and that the Treasurer could require the custodian to hold any principal payments or income for the Treasurer.

To effect any one of the four types of collateral transactions, deposits, withdrawals, substitutions, or transfers, the pledgor would be required to initiate such on a form prescribed by the Treasurer. Deposits of eligible collateral that are not made with restricted security types and substitutions of collateral that have at least equal market value would not require the prior approval of the Treasurer. Prior approval would be required by the Treasurer for a transfer, which occurs when a pledgor transfers the collateral either between accounts with the same custodian or between custodians. Additionally, the Treasurer’s prior approval would be required for a withdrawal of collateral, which occurs for example at the maturity date of the collateral.

If pledged collateral includes physical securities in registered forms which are in the name of the pledgor or the custodian, the pledgor or the custodian would be required to deliver to the Treasurer a separate certified power of attorney for each issue of securities, a separate bond assignment form as required by the bond agent or trustee, and certified copies of resolutions adopted by the pledgor's governing body authorizing the execution of these documents.

The pledgor would also be required to agree to be responsible for all costs incurred in the functioning of the collateral agreement and to not use a custodian that fails to complete the collateral agreement or fails to meet other requirements of the Treasurer regarding collateral.

Both the pledgor and the custodian would be required to agree to be subject to the jurisdiction of the courts of the state of Florida, or of courts of the United States located within the state of Florida for the purpose of any litigation arising out of this act; that any information, forms, or reports electronically transmitted to the Treasurer will have the same enforceability as a signed writing; to submit proof that authorized individuals executed the collateral agreement on behalf of the pledgor; and to be bound by any other provisions

found necessary for a perfected security interest in collateral under the Uniform Commercial Code.

The custodian of the pledgor also would be required to complete a collateral agreement and agree to not be responsible for ascertaining the value of the pledged securities or whether the pledged securities are eligible collateral; to hold the pledged collateral in a custody account and not enter into any agreement that would create an interest in or lien on that collateral in any manner in favor of any third party without the approval of the Treasurer; and that any lien that attaches to the collateral in favor of the custodian will not be superior or equal to the security interest of the Treasurer. The custodian is also required to process collateral transactions on forms prescribed by the Treasurer and obtain prior approval from the Treasurer for conducting certain transactions.

The Treasurer could require the deposit or transfer of collateral into a custodial account established under the Treasurer's name if at least one triggering event has occurred. The custodian used by Treasurer must meet certain requirements, all deposit transactions must be approved by the Treasurer, and all collateral must be in book-entry form.

Triggering events would include: the determination by the Treasurer that an immediate danger to the public health, safety, and welfare exists; the qualified public depository has not adopted adequate procedures for the accurate reporting and collateralization of public deposits; the qualified public depository or its operating subsidiary or the custodian fails to provide or allow inspection of documents relating to the pledged collateral; the custodian fails to hold income and principal payments made on securities held as collateral; the qualified public depository defaults or becomes insolvent; the qualified public depository fails to pay an administrative penalty; the qualified public depository fails to meet financial condition standards; the qualified public depository charges a withdrawal penalty to public depositors when the depository is suspended, disqualified, or withdrawn from the public deposit program; the qualified public depository fails to provide annual confirmation reports to the public depositor; the qualified public depository pledges insufficient or unacceptable collateral to cover public deposits; pledged collateral, other a proper substitution, is released without the prior approval of the Treasurer; the qualified public depository, custodian, or operating subsidiary, or agent violates any provision of the act and the Treasurer determines that such violation can be remedied by a move of collateral; the qualified public depository, custodian, operating subsidiary, or agent fails to timely cooperate in resolving problems by the date established by the Treasurer; the custodian fails to provide sufficient confirmation information; or events that would bring about an administrative or legal action by the Treasurer.

The Treasurer would also be given authority to adopt rules to implement this section.

Section 4 amends s. 280.13, F.S., to eliminate from the list of eligible collateral types: time deposits of the Federal Home Loan Bank and certificates of deposit. These types would no longer qualify as eligible collateral for use by a qualified public depository because the Treasurer would be unable to perfect security interest.

Section 5 amends s. 625.52, F.S., to specify that certificates of deposit issued by a lawfully organized bank, savings bank, or savings association that has its principal office or a branch office in the state would be eligible for deposit by insurers and agents as required for authority to transact business in the state.

Section 6 amends s. 660.27, relating to deposit of securities by trust companies and banks having trust powers, to require a trust company, bank, or association to provide the

Treasurer with the following written information: the full legal name of the entity; the employer identification number; the principal place of business; and the amount of capital stock and amount of required collateral.

The security deposit or pledge for each trust company, bank or association having trust powers would be limited to $500,000. Currently, if an entity with trust powers has its principal place of business in Florida, the security requirement may not exceed $500,000. Generally, entities that do not have their principal place of business in Florida must provide security in the amount of 25 percent of the issued and outstanding capital stock.

Every trust company, bank, or association as pledgor, with the approval of the Treasurer, is authorized to deposit eligible collateral with a custodian. The custodian may not be affiliated or related to the trust company, bank, or association.

Section 7 provides and effective date of July 1, 2000.

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:

None

D. FISCAL COMMENTS:

The Treasurer could be better able to seize the collateral pledged by a public depository in the event the public depository is financially unsound.

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

A. APPLICABILITY OF THE MANDATES PROVISION:

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

B. REDUCTION OF REVENUE RAISING AUTHORITY:

The bill does not reduce the authority that municipalities or counties have to raise revenue in the aggregate.

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

The bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

N/A

B. RULE-MAKING AUTHORITY:

The Treasurer would be given the authority to make rules to implement the provisions of this bill.

C. OTHER COMMENTS:

N/A

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On March 28, 2000, the Committee on Insurance adopted a “remove everything” amendment to HB 1831. In addition to making technical changes, such as correcting drafting oversights, this amendment would:

- require the Treasurer to notify the qualified public depository within one business day prior to directing the custodian to comply with the requests or orders of the Treasurer regarding liquidating collateral or transferring the collateral to the Treasurer.

- provide an exception from the collateral arrangements for a public depository depositing collateral with a Federal Reserve Bank. The agreement between the public depository and the Federal Reserve Bank may differ from the agreement set forth in s. 280.041(1), F.S., but would require the prior approval of the Treasurer.

- amend s. 660.27, F.S., to return the oversight of trust companies to the Treasurer. The $500,000 cap on the amount of security required to be deposited or pledged by certain trust institutions would be extended to all trust institutions. A trust company would be required to report certain information to the Treasurer on an annual basis. Eligible

collateral could be deposited with a custodian, subject to the approval of the Treasurer. Any collateral that is deposited would have to comply with the collateral provisions and agreements in s. 280.041(1) and (2).

VII. SIGNATURES:

COMMITTEE ON INSURANCE:

Prepared by:	Staff Director:
Meredith Woodrum Snowden	Stephen Hogge