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.)

BILL: CS/SB 2130

SPONSOR: Banking and Insurance Committee and Senator Rossin

SUBJECT: Public Deposits

DATE: March 21, 2000 REVISED: _____ _____ _____ _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Johnson	Deffenbaugh	BI	Favorable/CS
2.				
3.				
4.				
5.				

I. Summary:

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, pursuant to ch. 280, F.S.

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. Effective October 1, 1998, legislation was enacted, relating to the Uniform Commercial Code, which affected the Treasurer's security interest in pledged collateral held.

The Department of Banking and Finance is responsible for regulating state banks or associations with trust departments and trust companies under the provisions of ch. 660, F.S. However, every trust company and every state or national bank or state or federal association having trust powers is required to provide the Treasurer with a security deposit or pledge of security.

The committee substitute revises provisions relating to the qualified public depository program and security deposits by trust companies and banks and associations with trust powers as follows:

- Revises the qualified public deposit program to add specific language to the collateral agreements used in the program in order for the Treasurer to have a priority perfected security interest in the collateral pledged, in accordance with changes enacted in the Uniform Commercial Code. In addition, the bill identifies triggering events which would allow the Treasurer to assert a default has occurred under the collateral agreement and all collateral agreement provisions are added so that no provision could be questioned.

- Provides two additional requirements designed to better protect the public deposit program. Each qualified public depository is required to have a minimum of $100,000 collateral. Also, 20 percent additional collateral is required if the qualified public depository, due to hardship

reasons, cannot price their portfolio on the last day of the month. This provision would allow the Treasury to have adequate collateral pledged without the qualified public depository having to incur the expense of an additional pricing.

- Eliminates Federal Home Loan Bank time deposits and negotiable certificates of deposit as acceptable collateral types. The Federal Home Loan Bank time deposits are eliminated because the Treasurer is unable to perfect the security interest. Negotiable certificates of deposit are eliminated because it is unused collateral type and causes confusion with the nonnegotiable certificates of deposit that are not eligible as collateral.

- Excludes Federal Reserve banks from the standard collateral agreement, due to unacceptable provisions (including liability for the state and the waiver of sovereign rights) and establishes the possibility of entering into a separate agreement, with the approval of the Treasurer, that may require terms that are not consistent with qualified public depository program.

- Requires a trust company, bank, or association to provide the Treasurer with the following written information: 1) the full legal name of the entity; 2) the employer identification number; 3) the principal place of business; and 4) the amount of capital stock and amount of required collateral.

- Limits the security deposit or pledge for each trust company, bank or association having trust powers 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, an entity that does not have its principal place of business in Florida must provide a security deposit or pledge in the amount of 25 percent of the issued and outstanding capital stock.

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

This bill substantially amends the following sections of the Florida Statutes: 280.02, 280.04, 280.13, 625.52, and 660.57. This bill creates section 280.041, Florida Statutes.

II. Present Situation:

The Cabinet office of the Treasurer is established in s. 4, Art. IV, Fla. Const. The Treasurer is directed to keep all state funds and securities and to disburse state monies only upon the order of the Comptroller. Section 20.13, F.S., designates the Treasurer as the Insurance Commissioner, Treasurer, and State Fire Marshal and names the Treasurer as the head of the Department of Insurance. The law also directs the Treasurer to administer the Government Employees Deferred Compensation Plan through the Division of the Treasury.

Chapter 18, F.S., delineates many of the duties of the Treasurer. Among the duties assigned by law is the investment of state 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.

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.

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

The Uniform Commercial Code (UCC) consists of eleven articles (General Provisions; Sales; Commercial Paper; Bank Deposits and Collections; Letters of Credit; Bulk Transfers; Warehouse Receipts, Bills of Lading and Other Documents of Title; Investment Securities; Secured Transactions, Sales of Accounts and Chattel Paper; Effective Date and Repealer; Effective Date and Transition Provisions). It was created to promote uniformity among the states in all phases of a commercial transaction. Such uniformity is intended to facilitate interstate trade.

In 1965, ch. 678, F.S. was enacted to mirror Article 8 of the Uniform Commercial Code (UCC). Article 8 of the UCC and ch. 678, F.S. set ground rules for securities transfers, and for resolving disputes that arise when different people claim conflicting interests in a security. Other laws under which the securities markets operate include the Securities Exchange Act of 1934 and chapter 517, F.S. Beginning in 1987, the National Conference of Commissioners on Uniform State Laws (NCCUSL), the American Law Institution, the American Bar Association, and the Florida Bar drafted, reviewed, and recommended proposed revisions to Article 8 of the UCC. The NCCUSL was organized in 1892 to promote uniformity in state commercial codes. The NCCUSL is composed of commissioners from each state, the District of Columbia, and Puerto Rico.

Effective October 1, 1998, legislation was enacted to adopt UCC Articles 8 and 9. Chapters 678 and 679, F.S., were amended to adopt these changes and to modernize legislation by dealing with a previously unaddressed, yet fully functional, system of securities holdings. The system uses securities intermediaries, such as broker-dealers, who hold the actual security certificates on behalf of the owners of the certificates. The changes also reflect the increased use of electronic technology for the transfer of securities where the securities owner does not have physical possession of the security certificate.

The act also provides definitions and rules for determining whether an interest is a security or financial asset, including giving examples of interests that do or do not qualify as different types of securities (e.g., investment company security does not include insurance policies; interest in a

limited liability company is not security unless it is traded on securities exchanges or markets) and establishes the manner in which security interests in securities and other financial assets are acquired. Chapter 678, F.S., provides for the perfection of a security interest in an investment property by either obtaining control over the property or filing a financing statement. Chapter 679, F.S., addresses the rights of third parties and perfected and unperfected security interests.

Perfection by control means that the secured party has taken whatever steps are necessary to place itself in the 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 certificated securities, control is simply the delivery of possession of the certificate, with applicable endorsement. A security interest in an uncertificated security may be perfected by control by either: 1) the secured party becoming registered with the issuer as the holder of the uncertificated securities; or 2) the issuer, pledgor, and the secured party execute 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 control and by filing will protect the secured party against unperfected liens asserted by third parties, but the secured party who perfects its interest by obtaining control will have priority.

Perfection by filing provides that perfection may be obtained by: 1) execution of a security agreement between the pledgor and the secured party containing language that clearly creates a security interest; and 2) filing a financing statement covering the collateral described in the security agreement.

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, e.g., 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.

Section 625.52, F.S., requires insurance companies 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. The Department of Insurance has issued a legal opinion that states that the deposits held by the Treasurer, pursuant to s. 625.52, F.S., are not public deposits.

III. Effect of Proposed Changes:

Section 1. Amends s. 280.02, F.S., to define the various terms relating to public deposits.

“Affiliate,” is defined to mean an entity that is related through a parent corporation's controlling interest. The term also includes any financial institution holding company or any subsidiary or service corporation of such holding company.

“Book-entry form,” is defined to mean that securities are not represented by a paper certificate but represented by an account entry on the records of a depository trust clearing system, or in the case of U.S., government securities, a Federal Reserve Bank.

The term, “Collateral-pledging level,” for qualified public depositories, is amended to mean the percentage of collateral required to be pledged as provided in s. 280.04, F.S., *by a financial institution.*

“Operating subsidiary” is defined to mean the qualified public depository 100-percent owned corporation that has ownership of pledged collateral. The operating subsidiary may have no powers beyond those that its parent qualified public depository may itself exercise. The use of an operating subsidiary is at the discretion of the qualified public depository and must meet the Treasury's requirement.

“Pledged collateral” is defined to mean securities or cash held separately and distinctly by an eligible custodian for the benefit of the Treasurer to be used as security for Florida public deposits and includes maturity and call proceeds.

“Pledgor” is defined to mean the qualified public depository or the operating subsidiary.

The term, “Pool figure,” is defined to mean the total average monthly balances of public deposits held by all qualified public depositories during the immediately preceding 12-month period.

The term, “Public Deposit,” is expanded to include funds placed on deposit with savings banks. Securities, mutual funds, and similar types of investments are not considered public deposits and are not subject to the provisions of ch. 280, F.S.

“Treasurer's custody” is defined to mean a collateral arrangement governed by a contract between a designated Treasurer's custodian and the Treasurer. The collateral must in the Treasurer's name in order to perfect the security interest.

The term, “Triggering Events,” is defined to mean events set out in subsection 280.041(4), F.S., 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.

Section 2. Substantially rewords s. 280.04, F.S., relating to collateral for public deposits. The Treasurer is required to determine the collateral requirements and collateral pledging level for each qualified public depository following procedures adopted by rule, including numerical parameters for 25-percent, 50-percent, 125-percent, and 200-percent pledge levels based on nationally recognized financial rating services information and established financial performance guidelines.

The section prohibits a qualified public depository from retaining public deposits which are required to be secured unless it has deposited with the Treasurer eligible collateral at least equal to the *greater of*: 1) the average daily balance of public deposits that does not exceed the lesser of its capital accounts or 20 percent of the pool figure multiplied by the depository's collateral-pledging level, and the greater of 125 percent of the average daily balance of public deposits in excess of capital accounts; or 125 percent of the average daily balance of public accounts in excess of 20 percent of the pool figure; 2) 25 percent of the average monthly balance of public deposits; 3) 125 percent of the average daily balance of public deposits, if the qualified public depository has been established for less than 3 years; has experienced material decline in its capital accounts; or has an overall financial condition that is materially deteriorating; 4) 200 percent of an established maximum amount of public deposits that has been mutually agreed upon by and between the Treasurer and the qualified public depository; 5) Minimum required collateral of $100,000.

Additional collateral is required within 48 hours if public deposits are accepted that would increase the depository's average daily balance for the current month by 25 percent over the average daily balance of the previously reported month.

Each qualified public depository is required to value its collateral by: 1) using a nationally recognized source; 2) using market price, quality ratings, and pay-down factors as of the close of business on the last banking day in the reported month, or as of a date approved by the Treasurer; and 3) reporting any material decline in value that occurs before the date of mailing the monthly report to the Treasurer. Material decline is not defined.

Section 3. Creates s. 280.041, F.S., relating to collateral arrangements, agreements, provisions, and triggering events. With the approval of the Treasurer, a qualified public depository or operating subsidiary, as pledgor, may deposit eligible collateral with a custodian.
The Treasurer requires such a depository to submit a completed collateral agreement in which the pledgor agrees: 1) to own the pledged collateral; 2) to grant the Treasurer an interest in the pledged collateral; 3) to liquidate the collateral and submit the proceeds to the Treasurer upon request; 4) to grant the Treasurer an interest in the pledged collateral and to not enter into any other agreement that would create an interest in or lien on that collateral in favor of any third party without the written consent of the Treasurer; 5) to initiate collateral transactions on forms prescribed by the Treasurer, including deposit transactions of eligible collateral, such as security types that have restrictions that have been approved by the Treasurer in advance; 6) to initiate transfers of collateral between accounts at a custodian or between custodians with prior approval of the Treasurer; and 7) to initiate withdrawal transactions with prior approval of the Treasurer.

In the event pledged collateral includes physical securities in registered forms which are in the name of pledgor, the pledgor is required to deliver the following documents to the Treasurer: 1) a separate certified power of attorney for each issue of securities; 2) a separate bond assignment forms as required by the bond agent or trustee; and 3) certified copies of resolutions adopted by the pledgor's governing body authorizing the execution of these documents.

The pledgor also agrees to the following conditions: 1) to be responsible for all costs necessary to the functioning of the collateral agreement; 2) to not use a custodian that fails to complete the collateral agreement or fails to meet other requirements of the Treasurer regarding collateral;

3) 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; 4) any information, forms, or reports electronically transmitted to the Treasurer will have the same enforceability as a signed writing; 5) to submit proof that authorized individuals executed the collateral agreement on behalf of the pledgor; and 6) 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 is also required to complete a collateral agreement and agree to the following provisions: 1) not be responsible for ascertaining the value of the pledged securities or whether the pledged securities are eligible collateral; 2) will 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; 3) 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.

In the event pledged collateral includes physical securities in registered forms which are in the name of the custodian, the custodian is required to deliver the following documents to the Treasurer: 1) a separate certified power of attorney for each issue of securities; 2) a separate bond assignment forms as required by the bond agent or trustee; and 3) certified copies of resolutions adopted by the pledgor's governing body authorizing the execution of these documents.

The custodian also agrees to the following conditions: 1) that the pledgor is responsible for all costs necessary to the functioning of the collateral agreement; 2) to provide confirmation of pledged collateral upon request from the Treasurer; 3) 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; 4) any information, forms, or reports electronically transmitted to the Treasurer will have the same enforceability as a signed writing; 5) be responsible and liable to the Treasurer for any action of agents the custodian uses; 6) to allow the Treasurer to examine definitive pledged collateral and records; and 7) be bound by any other provisions found necessary for a perfected security interest in collateral under the Uniform Commercial Code.

The section allows qualified public depositories to enter into collateral agreements with Federal Reserve banks, upon approval of the Treasurer, that may require terms that are not consistent with the qualified public depository program, as stated in subsection (1).

The Treasurer may require deposit or transfer of collateral into a custodial account established in the Treasurer's name at a designated custodian, if: 1) one or more triggering events must have occurred; 2) the custodian used by Treasurer must meet certain requirements; 3) all deposit transactions require the approval of the Treasurer; and 4) all collateral must be in book-entry form.

The Treasurer may direct the custodian to deposit or transfer collateral upon the occurrence of one or more triggering events, provided that the Treasurer provides 48 hours' advance notice before directing such transaction. The triggering events include: 1) the Treasurer determines that

an immediate danger to the public health, safety, and welfare exists; 2) the qualified public depository has not adopted adequate procedures for the accurate reporting and collateralization of public deposits; 3) the qualified public depository or its operating subsidiary or the custodian fails to provide or allow inspection of documents relating to the pledged collateral; 4) the custodian fails to hold income and principal payments made on securities held as collateral; 5) the qualified public depository defaults or becomes insolvent; 6) the qualified public depository fails to pay an administrative penalty; 7) the qualified public depository fails to meet financial condition standards; 8) the qualified public depository charges a withdrawal penalty to public depositors when the depository is suspended, disqualified, or withdrawn from the public deposit program; 9) the qualified public depository fails to provide annual confirmation reports to the public depositor; 10) the qualified public depository pledges insufficient or unacceptable collateral to cover public deposits; 11) pledged collateral, other a proper substitution, is released without the prior approval of the Treasurer; 12) 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; 13) the qualified public depository, custodian, operating subsidiary, or agent fails to timely cooperate in resolving problems by the date established by the Treasurer; 14) the custodian fails to provide sufficient confirmation information; and 15) events that would bring about an administrative or legal action by the Treasurer.

The Treasurer is authorized to adopt rules to identify forms and establish procedures for collateral agreements and transactions.

Section 4. Amends s. 280.13, F.S., relating to collateral eligible for pledge by banks and savings associations, to eliminate time deposits and certificates of deposit.

Section 5. Amends s. 625.52, F.S., relating to securities eligible for deposit by insurers and agents transacting business in Florida, to specify what types of certificates of deposit are acceptable. The issuing bank, savings bank, or savings association must agree to the terms and conditions of the State Treasurer regarding the rights of the certificate of deposit and must have executed a written certificate of deposit agreement with the Treasurer. Such agreement is subject to the jurisdiction of the courts of this state, or those of the United States which are located in this state, for the purpose of any litigation arising out of this section.

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: 1) the full legal name of the entity; 2) the employer identification number; 3) the principal place of business; and 4) the amount of capital stock and amount of required collateral.

The section also limits the security deposit or pledge for each trust company, bank or association having trust powers 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 that this act will take effect July 1, 2000.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

State and national banks and associations having trust powers and trust companies would be subject to the same security deposit or pledge limitation of $500,000, regardless of whether the entity's principal place of business is located in Florida. Currently, an entity that does not have its principal place of business in Florida generally must provide a security deposit or pledge in the amount of 25 percent of the issued and outstanding capital stock.

C. Government Sector Impact:

By revising the qualified public deposit program to add specific language to the collateral agreements used in the program, this will allow the Treasurer to have a priority perfected security interest in the collateral pledged by qualified public depositories.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.