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DATE: April 2, 2001

**HOUSE OF REPRESENTATIVES
AS REVISED BY THE
COUNCIL ON COMPETITIVE COMMERCE
ANALYSIS**

BILL #: PCS/HB 991
RELATING TO: Funeral and Cemetery Services
SPONSOR(S): Council on Competitive Commerce and Representative Mayfield
TIED BILL(S): HB 1399

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

- (1) BANKING YEAS 8 NAYS 0
 - (2) GENERAL GOVERNMENT APPROPRIATIONS YEAS 14 NAYS 0
 - (3) COUNCIL ON COMPETITIVE COMMERCE
 - (4)
 - (5)
-

I. SUMMARY:

To protect the financial and often emotional investment consumers make when they contract for preneed funeral and cemetery services and merchandise, Ch. 497, F.S., requires the establishment of trust accounts, the procurement of surety bonds, or the submission of letters of credit to secure certain funds received in connection with such contracts. There are two types of surety bonds that are allowed by ss. 497.423 (performance) and 497.425 (payment), F.S. In essence, this bill provides two cutoff dates after which the bonding alternative in section 497.425, F.S., can no longer be used, holds harmless the bonding arrangements currently utilized by certificateholders, and does not allow those certificateholders to secure any other funds currently being held in trust as of the effective date of the bill. The bill also expands the list of financial institutions authorized to handle funeral and cemetery funds related to preneed and care and maintenance trust funds to include federal and state savings and loans.

This bill does not have a fiscal impact on state funds.

DIFFERENCE BETWEEN HB 991 AND PCS/HB 991:

The Proposed Council Substitute absorbs the amendment that is traveling with the bill and expands the list of financial institutions authorized to handle funeral and cemetery funds related to preneed and care and maintenance trust funds to include federal and state savings and loans. The PCS differs from the original bill in that it does not repeal the bonding alternatives but revises one of the alternatives by gradually phasing it out.

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:

To protect the financial and often emotional investment consumers make when they contract for preneed funeral and cemetery services and merchandise, Ch 497, F.S., requires the establishment of trust accounts or the procurement of surety bonds relating to the receipt of funds from such contracts. Chapter 497, F.S., also establishes a methodology by which specified cemeteries must set aside a portion of the cost of their services in a trust to provide for perpetual care and maintenance of gravesites.

Several sections of Ch. 497, F.S., provide a list of acceptable financial institutions which may handle care and maintenance and preneed contract trust funds. These are currently limited to those established by a trust business authorized under Ch. 660, F.S., or with a state or national bank. This list excludes federal or state savings and loan associations. At the time that the initial statutes were written, savings and loans did not have trust powers and only as of about five years ago were national savings and loans allowed to branch into Florida.

Section 497.405, F.S., requires all persons who may sell a preneed contract for services, merchandise or burial rights, to apply to the board for a valid certificate of authority, but makes very specific exemptions for trust institutions receiving funds in trust for the sale of a preneed contract, certain qualified Florida corporations, and certain churches offering specific preneed services that are located in counties with less than 960,000 in population on July 1, 1996. Section 497.407, F.S., requires each certificateholder to pay a one-time fee at an amount set by the board, not to exceed \$10, for each preneed contract entered into no later than 60 days after the end of each quarter. Fees are paid to the DBF and deposited into the Regulatory Trust Fund.

Section 497.417, F.S., requires all persons who collect funds under a preneed contract for funeral services or merchandise to deposit a prescribed amount of the monies collected into a trust account. These monies may not be used as loans to certificate holders or their affiliates nor can they be used as collateral.

In 1987, the Internal Revenue Service ruled (Ruling 87-127) that in certain situations where preneed contract purchasers retained some control and dominion over funds held in trust relating to their contracts, they would have to be provided with Form 1099s on an annual basis and they would be responsible for paying income tax on the earnings accrued on those funds. In 1988, the Florida Legislature amended Ch. 639, F.S., which governed preneed funeral and cemetery services contracts to provide an alternative to the trusting requirements so that the funeral or cemetery

company could be responsible for the tax on those assets. The provisions of former Ch. 639, F.S., were subsequently revised under Ch. 497, F.S.

One of the statutorily provided alternatives to establishing a preneed contract trust fund (s. 497.423, F.S.) allows a certificateholder to petition the Department of Banking and Finance's Board of Funeral and Cemetery Services to secure a surety bond in a prescribed amount. The bond must be conditioned in a way as to secure the "faithful performance of all conditions of any preneed contracts" the certificateholder is required to have covered by the bond. This includes refunds that are requested by consumers under certain conditions. The bond must also guarantee the financial responsibility of the company against defaults arising out of fulfilling preneed contracts. These types of surety bonds are commonly referred to as "performance bonds" because they must guaranty the performance of the service for which the preneed purchaser contracted.

Another alternative to the trust requirement is provided in s. 497.425, F.S. This section of the statutes provides that certificateholders may purchase a surety bond in a amount not less than the aggregate value of outstanding liabilities on undelivered preneed contracts for merchandise and services. These bonds are to be secured annually, and coverage increased or decreased depending on changes in the outstanding liabilities. These types of bonds are commonly known as "payment bonds" because the contract purchaser can file a claim against the surety company for payment. The bond must be maintained or the certificateholders must stop selling preneed contracts. In some cases, with board approval, a certificateholder may file a letter of credit in lieu of a surety bond.

Section 497.429, F.S., provides another alternative to the trusting agreements required on behalf of preneed contract purchasers. Under this section of the statutes, a certificate holder can establish a trust on behalf of the purchaser. In this instance, the certificateholder does not have any dominion or control over the trust or its assets until the contract has been fulfilled. Section 497.429, F.S., does provide for use of 10 percent of the funds collected or paid, 10 percent of liquidated damages, and for the cancellation of contracts under certain circumstances. Since earnings from the trust assets could have federal income tax implications for the purchaser, this section requires preneed contracts governed by this section to contain information relating to this tax implication.

At the current time, DBF reports that in excess of \$1,045,133,629 in preneed trust funds are maintained by approximately 330 certificateholders; four certificateholders, pursuant to s. 497.425, F.S., have payment-type surety bonds of approximately \$160,890,000 covering preneed contracts; and two certificateholders, pursuant to s. 497.425, F.S., have board-approved letters of credit. There are currently no companies with performance-type surety bonds held pursuant to 497.423, F.S. The department further reports that one licensee using a surety bond reorganized under Chapter 11 in July of 2000, and came out of bankruptcy in December of that year. To date, the department says that no claims against surety companies have been filed against certificateholders for failure to deliver merchandise and services upon need. Finally, the department reports that five certificate holders have failed to deposit sufficient funds in trust.

One provision for taking funds out of trust is that the merchandise contracted for has been delivered. Section 497.337(2), F.S., provides parameters for when merchandise and services may be considered delivered. Permanent outer burial receptacles that are delivered to the cemetery company may only be considered "delivered" if they are stored in a protected environment so that they won't deteriorate prior to the time the purchasers need them. For sales to cemetery companies and funeral establishments and only those sales, paragraph (2)(c) of s. 497.337, F.S., allows a manufacturer that has FCS board approved merchandise to elect to comply with the provisions of this section by annually submitting to the board proof of its financial responsibility, as established by the provisions in ss. 497.423, and 497.425, F.S.

C. EFFECT OF PROPOSED CHANGES:

See SECTION-BY-SECTION.

D. SECTION-BY-SECTION ANALYSIS:

Section 1 amends s. 497.201, F.S., conforming a reference to the revision of the list of financial institutions authorized to certify the establishment of care and maintenance trust funds (expanded to include federal and state savings and loan associations holding trust powers in the state in section 2 of this bill) provided in s. 497.237, F.S.

Section 2 amends s. 497.237, F.S., to provide that in addition to state banks that operate trust departments under Ch. 660, F.S., federal and state savings and loan associations holding trust powers in the state may establish the care and maintenance trust funds required for new cemeteries.

Section 3 amends s. 497.405, F.S., to conform a reference to the list of financial institutions expanded in section 4 of this bill, that are authorized to handle preneed contract funds.

Section 4 amends s. 497.417, F.S., to provide that in addition to state banks that operate trust departments under Ch. 660, F.S., federal and state savings and loan associations holding trust powers in the state may establish the trust funds required for licensees that offer preneed contracts. This conforms the treatment of this trust fund requirement to that of the care and maintenance trust fund requirements revised in section 2 of this bill.

This section also revises subsection (5) of s. 497.417, F.S., relating to the authority given to a preneed funeral and cemetery services contract seller/certificateholder to revest in itself title to trust assets or its pro rata share of such assets if it has procured a surety bond under s. 497.423, F.S., or s. 497.425, F.S. The reference to the bonding provisions in s. 497.425, F.S., is conformed to mirror the limitations this bill makes on that bonding authority. Effectively this would limit the ability of certificateholders to revest in themselves title to trust funds to only those trust funds they have already secured by bonds as of the effective date of this bill (7/1/01) unless the company can be identified as currently securing \$100,000,000 in bonds. Such a company would have its authority limited to funds it currently has bonded and those relating to contracts written up until December 31, 2004. Certificateholder's funds that are residing in trusts as of July 1, 2001, must remain there. These provisions leave open certain alternatives for the purpose of compliance with federal income tax requirements.

Section 5 amends s. 497.425, F.S., to revise the authority given to certificateholders to procure payment-type surety bonds in lieu of holding the prescribed preneed contract funds in trust. The revision allows certain certificateholders to continue to use the alternative authorized under s. 497.425, F.S., of securing funds by bond rather than by trust, on contracts written prior to July 1, 2001, but relates only to those funds not held in trust as of July 1, 2001. A specific provision is made for a certificateholder that is authorized to do business in Florida and that currently has \$100,000,000 secured by bonds. This particular certificateholder is allowed to use this alternative of securing funds by bond rather than by trust, on contracts written prior to December 31, 2004, but relates only to those funds not held in trust as of July 1, 2001. In summary this revision provides two cutoff dates after which the bonding alternative in section 497.425 can no longer be used, holds harmless the bonding arrangements currently utilized by certificateholders, and does not allow those certificateholders to secure any other funds currently being held in trust as of the effective date of the bill.

Section 6 amends s. 497.429, F.S., to conform a reference to the list of financial institutions authorized to certify the establishment of preneed trust funds expanded in section 4 of this bill.

Section 7 provides that this act will take effect July 1, 2001.

II. 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:

N/A

2. Expenditures:

N/A

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

As reported by the Department of Banking and Finance, there are four funeral and cemetery service companies that have procured annual surety bonds under s. 497.425, F.S., one of which has a total bonded liability of \$100,000,000. The gradual phase out of the bonding alternative in s. 497.425, F.S., should not cause undue financial hardship on certificateholders.

D. FISCAL COMMENTS:

N/A

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

A. APPLICABILITY OF THE MANDATES PROVISION:

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

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

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

IV. COMMENTS:

A. CONSTITUTIONAL ISSUES:

None found.

B. RULE-MAKING AUTHORITY:

N/A

C. OTHER COMMENTS:

N/A

V. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On March 20, 2001, the Committee on Banking adopted a strike everything amendment with title that:

Allows certain certificate holders under Chapter 497, to continue to use the alternative authorized under Section 497.425, of securing funds by bond rather than by trust, on contracts written prior to July 1, 2001, but relates only to those funds not held in trust as of July 1, 2001.

Allows other certificate holders (as specifically identified by the amendment) to use this alternative of securing funds by bond rather than by trust, on contracts written prior to December 31, 2004, but relates only to those funds not held in trust as of July 1, 2001.

In essence this amendment provides two cutoff dates after which the bonding alternative in section 497.425 can no longer be used, holds harmless the bonding arrangements currently utilized by certificate holders, and does not allow those certificate holders to secure any other funds currently being held in trust as of the effective date of the bill.

The Proposed Council Substitute absorbs the amendment that is traveling with the bill and expands the list of financial institutions authorized to handle funeral and cemetery funds related to preneed and care and maintenance trust funds to include federal and state savings and loans. The PCS differs from the original bill in that it does not repeal the bonding alternatives but revises one of the alternatives by gradually phasing it out.

VI. SIGNATURES:

COMMITTEE ON BANKING:

Prepared by:

Susan F. Cutchins

Staff Director:

Susan F. Cutchins

AS REVISED BY THE COMMITTEE ON GENERAL GOVERNMENT APPROPRIATIONS:

Prepared by:

Juliette Noble

Staff Director:

Lynn Dixon

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AS FURTHER REVISED BY THE COUNCIL ON COMPETITIVE COMMERCE:

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