

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** CS/HB 825 Family Trust Companies  
**SPONSOR(S):** Insurance & Banking Subcommittee; Roberson  
**TIED BILLS:** **IDEN./SIM. BILLS:** CS/SB 568

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	12 Y, 0 N, As CS	Bauer	Cooper
2) Regulatory Affairs Committee	12 Y, 0 N	Bauer	Hamon

### SUMMARY ANALYSIS

In 2014, the Florida Legislature created the Florida Family Trust Company Act (ch. 662, F.S., "the Act"). Effective October 1, 2015, the Act allows families to form unlicensed, licensed, and foreign licensed private family trust companies (FTCs), subject to certain regulatory requirements. The Act will be enforced by the Office of Financial Regulation (OFR), which charters and regulates entities engaging in financial institution business in Florida, including public, commercial trust companies.

The bill modifies and clarifies a number of the Act's requirements of licensed FTCs, unlicensed FTCs, and foreign licensed FTCs. The bill:

- Provides that OFR must conduct an examination of a licensed FTC every 36 months instead of the current 18 months;
- Removes the requirement that OFR conduct examinations of unlicensed FTCs;
- Requires that judicial determination of a breach of fiduciary duty or trust before the OFR may enter a cease and desist order, and clarifies that a FTC has an opportunity for an administrative hearing before the OFR may revoke a FTC's license;
- Requires all FTCs in operation on October 1, 2015, to either apply for the appropriate FTC license or registration, or cease doing business in this state by December 30, 2015;
- Clarifies that OFR is responsible for the regulation, supervision, and examinations of licensed FTCs, but limits the OFR's role over unlicensed or foreign FTCs to ensuring that services provided by such companies are provided only to family members and to determining conformity with the Act;
- Requires the management of a licensed FTC to have at least three directors or managers and requires that at least one of those directors or managers be a Florida resident;
- Provides that a FTC registration application must state that trust operations will comply with statutory provisions relating to organizational documents, minimum capital requirements, and segregated books, records, and assets;
- Provides that the designated relatives in a licensed FTC may not have a common ancestor within three generations, instead of the current five generations;
- Requires that a registration application for a foreign licensed FTC must provide proof that the company is in compliance with the FTC laws and regulations of its principal jurisdiction;
- Requires amendments to certificates of formation or certificates of organization to be submitted to the OFR at least 30 days before it is filed or effective; and
- Allows FTCs to file annual renewal applications within 45 days of the end of each calendar year.

The bill does not appear to have a fiscal impact on state and local governments. The bill may have a positive impact on the private sector.

The bill is effective October 1, 2015.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

##### **Trusts**

A trust is generally defined as, "a fiduciary relationship with respect to property, subjecting the person by whom the title to the property is held to equitable duties to deal with the property for the benefit of another person, which arises as a result of a manifestation of an intention to create it."<sup>1</sup> A trust must have three interest holders - a settlor (also called a "grantor"), a trustee, and a beneficiary. The settlor is the party creating the trust. The beneficiary has an equitable interest in property subject to trust, enjoying the benefit of the administration of the trust by a trustee.<sup>2</sup> The trustee holds legal title to the property held in trust for the benefit of the beneficiary.<sup>3</sup> A bank with trust powers or a trust company may offer its services to the general public to serve as trustee of private trusts.

##### **Background: Florida Family Trust Company Act**

In 2014, the Florida Legislature created the Florida Family Trust Company Act (ch. 662, F.S., "the Act").<sup>4</sup> Effective October 1, 2015, the Act allows families to form unlicensed, licensed, and foreign licensed private family trust companies (FTCs), subject to certain regulatory requirements that will be enforced by the Office of Financial Regulation (OFR), which charters and regulates entities engaging in financial institution business in Florida, which include public, commercial trust companies, in accordance with the Florida Financial Institutions Codes (Codes).<sup>5</sup>

Families may prefer to form a private FTC (instead of using individual or institutional trustees) for a variety of reasons, such as tax and regulatory advantages, privacy, flexibility, and self-governance of the family's financial affairs. At least 14 other states currently have statutes governing the organization and operation of FTCs.

In general, an FTC is an entity which provides trust services similar to those provided by an individual or an institutional trustee. This includes serving as a trustee of trusts held for the benefit of the family members, as well as providing other fiduciary, investment advisory, wealth management, and administrative services to the family. A Florida FTC must be owned exclusively by family members and may not provide fiduciary services to the public.<sup>6</sup> The Act's three FTC types are:<sup>7</sup>

##### 1. *(Unlicensed) Family trust company*

A FTC is a corporation or limited liability company exclusively owned by one or more family members, organized or qualified to do business in Florida, and acts as a fiduciary for one or more family members. A FTC may not serve as a fiduciary for a non-family member, except that it may provide such fiduciary services for up to 35 individuals who are not family members, but who are current or former employees of the FTC or of trusts, companies, or other entities that are family members.

##### 2. *Foreign licensed family trust company*

A foreign licensed FTC has its principal place of business outside of Florida, and is licensed, operating, and supervised by a state other than Florida or by the District of Columbia, and is not owned by or a

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<sup>1</sup> 55A Fla.Jur.2d Trusts s.1; *see also* s. 731.201(38), F.S.

<sup>2</sup> *Id.*

<sup>3</sup> 55A Fla.Jur.2d Trusts s.1.

<sup>4</sup> Ch. 2014-97, Laws of Fla.

<sup>5</sup> The Codes consist of ch. 655 (Financial Institutions), ch. 657 (Credit Unions), ch. 658 (Banks and Trust Companies), ch. 660 (Trust Business), ch. 663 (International Banking), ch. 665 (Associations), and ch. 667 (Savings Banks), F.S.

<sup>6</sup> s. 662.102, F.S.

<sup>7</sup> s. 662.111(12), (15), and 16), F.S.

subsidiary of a business entity that is organized in or licensed by any foreign country as defined by the international banking chapter of the Codes.<sup>8</sup>

### 3. *Licensed family trust company*

A licensed FTC operates under a current (not revoked or suspended) license issued by the OFR.

The Act contains regulatory requirements relating to:

- Initial and renewal licensure and registration,
- Acts authorizing the OFR to take action against a FTC's license or registration, including cease and desist authority,
- Qualifications for directors, officers, managers or managerial members of any FTC type,
- Organizational and management authority for FTCs,
- Capital requirements for FTCs with a principal place of business in Florida, and
- Investigation, examination, and enforcement authority by the OFR, including cease and desist authority.

## **Current Situation**

According to proponents of the Act and the bill, a number of family offices in Florida have indicated that the Act is not workable in its current form, namely due to the Act's examination requirements that would be intrusive into private family arrangements, and may exceed what is minimally required to avoid triggering the application of certain federal securities laws.<sup>9</sup> Currently, the Act requires that OFR conduct an examination of all FTC types at least once every 18 months.<sup>10</sup>

### **Deficiencies in the Act for unlicensed FTCs and foreign licensed FTCs**

Section 662.141(1), F.S., requires OFR to conduct mandatory examinations of each unlicensed FTC once every 18 months in order to determine that it is operating as an unlicensed FTC within the meaning of the Act. It is unclear how OFR will conduct such examinations, but each review of an unlicensed FTC will necessarily require a review of private family trust instruments and financial arrangements. The majority of FTCs in existence in other jurisdictions choose to organize as unlicensed, unregulated FTCs, due to the desire to keep family arrangements private and to avoid being subjected to intrusive examinations. Examinations of unlicensed FTCs are inconsistent with the purpose of the Act, which provides that "unlike trust companies formed under chapter 658, there is no public interest to be served outside of ensuring that fiduciary activities performed by a family trust company are restricted to family members."<sup>11</sup> If unlicensed FTCs are subject to mandatory OFR examinations, then Florida's comparatively intrusive examination requirements may deter unlicensed FTCs located in other states, as well as family offices currently operating in Florida, from organizing as an unlicensed FTC in Florida.<sup>12</sup>

### **Deficiencies in the Act for licensed FTCs**

According to the proponents, there is no public interest served by having OFR regulate FTCs. Nevertheless, a small number of FTCs may desire OFR supervision for any of a number of reasons including family governance issues, federal income tax considerations and exemption from SEC regulation under the federal Investment Adviser Act of 1940. A family office may need to register with the SEC as an "investment adviser" if it does not fit within the SEC's definition of "family office."<sup>13</sup> An "investment adviser" is any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities.<sup>14</sup> However, the SEC has somewhat restrictively defined "family office," and for many

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<sup>8</sup> See s. 663.01(3), F.S.

<sup>9</sup> Real Property, Probate and Trust Law Section (RPPTL) of the Florida Bar, *White Paper on Proposed Changes to the Florida Family Trust Company Act*, pp. 2-3 (on file with the Insurance & Banking Subcommittee staff).

<sup>10</sup> s. 662.141(1), F.S.

<sup>11</sup> s. 662.102, F.S.

<sup>12</sup> RPPTL White Paper, pp. 3-4.

<sup>13</sup> 15 U.S.C. §80-2(a)(11).

<sup>14</sup> 15 U.S.C. §80b-2(a)(11).

families this definition would exclude certain in-laws, aunts and uncles, and cousins. Thus, a family office serving those individuals would typically fail the SEC's "family office" definition, subjecting it to burdensome SEC registration as an investment adviser.

SEC registration requirements and regulations may include: (1) filing a Form ADV with the SEC, which must be kept current with periodic updates; (2) annual filings with the SEC of an audited balance sheet; (3) undergoing an annual surprise examination by an independent public accountant to verify client assets; and (4) inspections and examinations by SEC staff.<sup>15</sup> While the 1940 Investment Adviser Act generally protects the disclosure of client identity, investments or affairs and the fact of examination or investigation by the SEC, it does make public information contained in registration applications, reports, and amendments thereto filed with the SEC, unless the SEC "finds that public disclosure is neither necessary nor appropriate in the public interest or for the protection of investors."<sup>16</sup>

The Act was written with the intention that a licensed FTC would not be required to register as an "investment adviser" under the 1940 Investment Advisers Act. In addition to exempting family offices, the 1940 Act excludes "banks" from the definition of "investment adviser," and includes "trust company[ies]... doing a substantial portion of the business which consists of receiving deposits or exercising fiduciary powers similar to those permitted to national banks...and which is supervised and examined by State or Federal authority having supervision over banks...and which is not operated for the purpose of evading the provisions of this subchapter"<sup>17</sup> (emphasis added). It was believed that OFR regulation of licensed FTCs under the Act would be sufficient to constitute "supervised and examined" within the meaning of this so-called "bank exemption" from SEC regulation under the 1940 Act.

The view of SEC regulation experts regarding whether state "supervision and examination" is sufficient to allow an FTC to qualify for the "bank exemption" has evolved since the enactment of chapter 662. Currently, the Act requires OFR to examine licensed FTCs once every 18 months, but only for compliance with very specific provisions of the Act.<sup>18</sup> Moreover, licensed FTCs may be able to satisfy examination requirements through the submission of audits conducted by certified public accounting firms. Experts in the field of SEC regulation now believe that in order to qualify for the "bank exemption," a licensed FTC must be regulated and examined in substantially the same manner as a public trust company, although not necessarily with the same frequency.<sup>19</sup> The regulation and examination of licensed FTCs under the current Act falls short of this standard, which would make them unlikely to qualify for the "bank exemption" from investment advisor registration requirements.<sup>20</sup>

## **Effect of the Bill**

In addition to addressing the deficiencies in the Act's examination requirements as discussed above, the bill clarifies a number of other provisions in the Act.

### **Examinations of FTCs**

**Section 1** of the bill amends 662.102, F.S., which describes the purpose of the Act, to clarify that OFR will regulate, supervise and examine only those FTCs which choose to organize as licensed FTCs.

**Section 3** of the bill creates s. 662.113, F.S., to clarify that the financial institutions codes do not apply to FTCs unless otherwise indicated in the Act, although it does not limit the OFR's ability to investigate any entity to ensure that it is not in violation with the Act or the Codes. The Act is intended to be a stand-alone framework for FTC governance.

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<sup>15</sup> 15 U.S.C. §§80b-3 and 80b-4; *see also* SECURITIES & EXCHANGE COMMISSION, *How to Register as an Investment Adviser*, at <http://www.sec.gov/divisions/investment/iaregulation/regia.htm> (last viewed Mar. 1, 2015).

<sup>16</sup> 15 U.S.C. §80b-10.

<sup>17</sup> *See* 15 U.S.C. §80b-2(a)(11)(A) (definition of "investment adviser") and 15 U.S.C. §80b-2(a)(2)(C) (definition of "bank").

<sup>18</sup> s. 662.141, F.S.

<sup>19</sup> Section 655.045(1), F.S., requires the OFR to examine each state financial institution at least every 18 months. While OFR may accept an examination from an appropriate federal regulator or conduct joint or concurrent examinations with federal regulators, OFR must conduct its own independent examination at least once during each 36-month period beginning July 1, 2014.

<sup>20</sup> RPPTL White Paper, pp. 4-6.

**Section 11** of the bill amends s. 662.141, F.S., to expand the scope of OFR examinations of *licensed FTCs* to make them sufficiently similar to examinations of public trust companies in order for to qualify for the “bank exemption” from SEC regulation under the 1940 Act. Although examinations of licensed FTCs will be more rigorous, the bill provides that they will occur only once every 36 months rather than once every 18 months. The bill also clarifies that *unlicensed FTCs and foreign licensed FTCs* are subject to OFR examinations to the extent necessary to determine whether they have engaged in certain prohibited activities or have advertised services to the general public, and makes some drafting changes to reorder subsections.

#### Licensure, Registration, and Regulation of FTCs

**Section 5** of the bill amends s. 662.1215, F.S., to specify that the OFR’s initial investigation of applicants seeking to become licensed FTCs includes a confirmation that the proposed FTC’s management structure complies with s. 662.125, F.S., which contains requirements for directors and officers.

**Section 6** of the bill amends s. 662.122, F.S., to add cross-references (regarding organizational documents and minimum capital requirements) for the registration process for unlicensed FTCs and foreign licensed FTCs. It also adds a requirement to this statute that every foreign licensed FTC provide proof it is in compliance with the FTC laws and regulations of its principal jurisdiction.

**Section 7** of the bill amends s. 662.1225, F.S., to clarify that a foreign licensed FTC must be in compliance with the FTC laws and regulations of its principal jurisdiction as a condition to operating in this state. The bill also provides that companies operating as a FTC as of October 1, 2015, must apply for licensure or registration on or before December 30, 2015, or cease doing business in this state.

**Section 9** of the bill amends s. 662.128, F.S., to allow FTCs to file their annual renewals within 45 days after the end of the calendar year, rather than the 30 days currently required in statute. The annual renewal application is anticipated to be a somewhat complex document requiring more than 30 days to prepare. The bill also clarifies that the license renewal application’s verified statement be made by the FTC’s authorized representative.

**Section 12** of the bill amends s. 662.142, F.S., which sets forth the grounds for revocation of a licensed FTC’s license by OFR, including an act of commission or omission that is determined by a court of competent jurisdiction to be a breach of trust or fiduciary duty. If OFR finds that an FTC has committed an act constituting a breach of trust or fiduciary duty, OFR may enter an order immediately revoking the FTCs license. The bill modifies s. 662.142, F.S., to account for the licensed FTC’s administrative hearing rights under the Administrative Procedure Act (ch. 120, F.S.), and clarifies that the OFR may enter an order of revocation after a hearing has not been timely requested pursuant to ss. 120.569 and 120.57 or if a hearing is held and it has been determined that the licensed FTC has committed any violations enumerated in subsection (1).

**Section 13** of the bill amends s. 662.143, F.S., allows OFR to issue a cease and desist order upon an FTC in the event of certain violations of the Act, including an act of commission or omission that OFR has reason to believe constitutes a breach of trust or a breach of fiduciary duty. The bill modifies s. 662.143, F.S., to require that an act of commission or omission be judicially determined to be a breach of trust or fiduciary duty prior to OFR issuing a cease and desist order.

**Section 17** of the bill amends s. 662.151, F.S., to relocate existing language to s. 662.1225, F.S. (which is amended by Section 7 of the bill), regarding general FTC requirements. The language requires that an FTC that is in operation prior to October 1, 2015 must apply for licensure as a licensed FTC or register as an unlicensed FTC within 90 days of the Act’s effective date (i.e., January 1, 2016), or cease doing business in this state. The bill clarifies that FTCs in operation as of October 1, 2015 must, on or before December 30, 2015, apply for the appropriate FTC licensure or registration.

#### FTC Organization & Operation

**Section 2** of the bill amends s. 662.111, F.S., is the definition of “officer,” and includes non-director individuals who participate in the FTC’s major policymaking functions. The definition contains a presumption that certain officers, such as the president, the chief financial officer, etc., are *executive* officers, unless excluded from major policymaking function by board resolution, bylaws, or operating agreement, as well as actual non-participation in those major policymaking functions by the individual. The bill amends this definition to eliminate reference to an “executive” officer.

**Section 4** of the bill amends s. 662.120(2), F.S., which limits licensed FTCs to two “designated relatives,” so long as the designated relatives do not have a common ancestor within five generations. The bill amends this provision to prohibit the two designated relatives from having a common ancestor within *three* generations.

**Section 8** of the bill amends s. 662.123, F.S., sets forth certain requirements for organizational documents for an FTC and requires an FTC to submit any proposed changes to its articles of incorporation, articles of organization, bylaws, or articles of organization of a limited liability company to OFR for review at least 30 days before an amendment is to become effective. The bill adds certificates of formation or certificates of organization to these organizational documents requiring OFR’s preapproval, but eliminates bylaws and articles of organization. According to the proponents, amendments to a FTC’s bylaws or articles of organization should not require approval from OFR, because the overwhelming majority of such instruments typically involve ministerial acts of day-to-day governance.<sup>21</sup>

**Section 10** of the bill amends s. 662.132, F.S., which sets forth restrictions on the purchases of bonds or other security instruments by an FTC from an affiliate of the FTC. The bill deletes the reference with the term “affiliate” in order to avoid confusion with the defined term “family affiliate” in s. 662.111, F.S. The bill substitutes “parent or subsidiary company” in place of the term “affiliate.” Additionally, the bill substitutes the more legally accurate term “broker-dealer” instead of “distributor” to describe permissible investment transactions for FTCs.

**Section 14** of the bill amends s. 662.143, F.S., to provide procedures for reinstating a FTC license or registration through the filing of a renewal application and payment of fees and fines.

**Sections 15 and 16** of the bill make technical changes to ss. 662.145 and 662.150, F.S.

#### B. SECTION DIRECTORY:

Section 1. Amends s. 662.102, F.S., relating to the purpose of the Family Trust Company Act.

Section 2. Amends s. 662.111, F.S., relating to definitions.

Section 3. Creates s. 662.113, F.S., relating to applicability of other chapters of the financial institutions codes.

Section 4. Amends s. 662.120, F.S., relating to maximum number of designated relatives.

Section 5. Amends s. 662.1215, F.S., relating to investigation of license applicants.

Section 6. Amends s. 662.122, F.S., relating to registration of a family trust company or a foreign licensed family trust company.

Section 7. Amends s. 662.1225, F.S., relating to requirements for a family trust company, licensed family trust company, and foreign licensed family trust company.

Section 8. Amends s. 662.123, F.S., relating to organizational documents; use of term “family trust” in name.

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<sup>21</sup> RPPTL White Paper, p. 7.  
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- Section 9. Amends s. 662.128, F.S., relating to annual renewal.
- Section 10. Amends s. 662.132, F.S., relating to investments.
- Section 11. Amends s. 662.141, F.S., relating to examination, investigations, and fees.
- Section 12. Amends s. 662.142, F.S., relating to revocation of license.
- Section 13. Amends s. 662.143, F.S., relating to cease and desist authority.
- Section 14. Amends s. 662.144, F.S., relating to failure to submit required report; fines.
- Section 15. Amends s. 662.145, F.S., relating to grounds for removal.
- Section 16. Amends s. 662.150, F.S., relating to domestication of a foreign family trust company.
- Section 17. Amends s. 662.151, F.S., relating to registration of a foreign licensed family trust company.
- Section 18. Provides an effective date of October 1, 2015.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

### A. FISCAL IMPACT ON STATE GOVERNMENT:

#### 1. Revenues:

According to the bill's proponents, the bill should not have a fiscal impact on state and local governments. The bill's elimination and simplification of OFR examination requirements on licensed and non-licensed FTCs, respectively, should be revenue neutral or revenue positive. The application fees for establishing FTCs, annual certification and other fees are anticipated to offset OFR's costs in regulating licensed FTCs.<sup>22</sup>

OFR does not anticipate that the bill will have a fiscal impact to state government.<sup>23</sup>

#### 2. Expenditures:

See Revenues, above.

### B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

#### 1. Revenues:

None.

#### 2. Expenditures:

None.

### C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

According to the proponents, the bill should help attract high net worth families to choose Florida as a jurisdiction to establish family trust companies.<sup>24</sup>

### D. FISCAL COMMENTS:

See above.

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<sup>22</sup> RPPTL White Paper, p. 10.

<sup>23</sup> Office of Financial Regulation, Agency Analysis of 2015 House Bill 825, p. 5 (Mar. 3, 2015).

<sup>24</sup> *Id.*

### III. COMMENTS

#### A. CONSTITUTIONAL ISSUES:

##### 1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

##### 2. Other:

None.

#### B. RULE-MAKING AUTHORITY:

The bill does not provide any new rulemaking authority. The bill reorganizes s. 662.141, F.S., to move existing rulemaking authority to the Financial Services Commission in subsection (3) (regarding records and requirements necessary to demonstrate conformity with the Act) to subsection (6).

#### C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

### IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On March 10, 2015, the Insurance Banking & Subcommittee considered and adopted a strike-all amendment and reported the bill favorably as a committee substitute. The amendment made the bill identical to the Senate companion bill (CS/SB 658) to include additional clarifying changes to the Act:

- Clarifies that OFR may investigate any entity to ensure that it is not in violation with the Act or the financial institutions codes.
- Clarifies and reorganizes language requiring family trust companies to apply for licensure or registration on or before December 30, 2015, or cease operating in this state.
- Substitutes the more legally accurate term of “broker-dealer” instead of “distributor” to describe permissible investments for FTCs.
- Clarifies that unlicensed and foreign FTCs are subject to OFR examinations to the extent necessary to determine whether they have engaged in certain prohibited activities or have advertised services to the general public.
- Expands the scope of OFR examinations of licensed family trust companies so that such examinations are comparable to OFR examinations of public trust companies.
- Provides procedures for reinstatement of a family trust company upon filing of renewal application and payment of fees and fines.
- Provides that any family trust company that fails to renew or reinstate must wind up its affairs by a date certain.

The staff analysis has been updated to reflect the committee substitute as passed by the Insurance & Banking Subcommittee.