HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: PCS for HB 1373 Public Depositories
SPONSOR(S): Insurance & Banking Subcommittee
TIED BILLS: **IDEN./SIM. BILLS:**

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
Orig. Comm.: Insurance & Banking Subcommittee		Hinshelwood	Luczynski

SUMMARY ANALYSIS

State and local governments are required, unless exempted by law, to deposit public funds in a qualified public depository (QPD) pursuant to the Florida Security for Public Deposits Act (Act), which is administered by the Chief Financial Officer (CFO) and the Department of Financial Services (DFS). Before a QPD accepts or retains a public deposit, it must deposit collateral with an approved custodian in an amount commensurate with the amount of public deposits held and commensurate with the financial stability of the financial institution. Currently, banks, savings banks, and savings associations are the only types of financial institutions eligible to be a QPD or a custodian for a QPD's pledged collateral.

The bill makes the following amendments to the Act:

- Makes state-chartered and federally-chartered credit unions eligible to become QPDs and custodians of pledged collateral;
- Provides criteria that a credit union must meet before the CFO can designate a credit union as a QPD;
- Creates separate mutual responsibility and contingent liability provisions for credit unions, in order to prevent credit unions from sharing contingent liability with banks, and vice versa; and
- Requires the CFO to segregate and separately account for any collateral proceeds, assessments, or administrative penalties attributable to a credit union from those attributable to any bank, savings bank, or savings association.

The bill has an indeterminate fiscal impact on revenues for the state. The bill requires state expenditures of $78,699 in the first fiscal year and $74,433 in subsequent fiscal years for one FTE position; $5,728 in recurring expenditures for additional subscriptions to financial ranking services; and $188,650 in non-recurring expenditures for modifications to the computer application utilized in the administration of the public deposits program. The bill has an indeterminate fiscal impact on local governments and the private sector.

The bill provides an effective date of July 1, 2018.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Background

Public Depositories

State and local governments are required, unless exempted by law, to deposit public funds in a qualified public depository (QPD)[1] pursuant to the Florida Security for Public Deposits Act (Act).[2] A QPD is any bank, savings bank, or savings association that:

- Is organized and exists under the laws of the United States, the laws of this state or any other state or territory of the United States (i.e., state or federally chartered);
- Has its principal place of business in this state or has a branch office in this state which is authorized under the laws of this state or of the United States to receive deposits in this state;
- Has deposit insurance under the provision of the Federal Deposit Insurance Act, as amended, 12 U.S.C. ss. 1811 et seq.;
- Has procedures and practices for accurate identification, classification, reporting, and collateralization of public deposits;
- Meets all the requirements of the Act; and
- Has been designated by the Chief Financial Officer (CFO) as a qualified public depository.[3]

Upon approval by the CFO, these banks, savings banks, and savings associations may accept "public deposits"[4] from state and local governments. The Act does not permit credit unions to become QPDs, due to their absence from the definition of "qualified public depository." Currently, there are 142 active QPDs in this state.[5]

Before a QPD accepts or retains a public deposit, it must deposit collateral with an approved custodian in an amount commensurate with the amount of public deposits held and commensurate with the financial stability of the financial institution.[6] The Act's collateral requirements protect public deposits against loss in the event of certain triggering events, most notably, a QPD's insolvency or default.[7] Losses are satisfied first through the standard maximum federal deposit insurance of $250,000,[8] and then through the CFO's demand for payment under letters of credit or the sale of collateral pledged or deposited by the defaulting QPD. Any shortfall would then be covered by the CFO's authority to impose assessments against the other solvent QPDs, who must agree to share mutual responsibility and contingent liability as a condition of acting as a QPD.[9]

A "custodian" can be any state or federally chartered bank, savings association, and trust company that is approved by the CFO to hold the collateral that QPDs have pledged to secure public deposits.[10]

[1] s. 280.03(1)(b), F.S.
[2] ch. 280, F.S.
[3] s. 280.02(26), F.S.
[4] Public deposits include, but are not limited to, time deposit accounts, demand deposit accounts, and nonnegotiable certificates of deposits, but do not include moneys in deposit notes, securities, mutual funds, and similar investments. s. 280.02(23), F.S.
[5] A list of active QPDs is available at: http://www.myfloridacfo.com/division/treasury/collateralmanagement/documents/ListofActiveQPDs.pdf (last visited Mar. 24, 2017).
[6] s. 280.04, F.S. *See also* ch. 69C-2, F.A.C.
[7] s. 280.041(6), F.S.
[8] 12 U.S.C. § 1821(a)(1)(E).
[9] s. 280.07, F.S.
[10] ss. 280.02(10) and 280.041(1)(a), F.S.

These are referred to as "regular" custodians. Subject to specific requirements, QPDs also have the option to pledge their collateral with custodians who are bound under a distinct custody contract directly with the CFO ("CFO's custodians");[11] pursuant to an agreement with a Federal Reserve Bank;[12] or may use a Federal Home Loan Bank letter of credit that names the CFO as beneficiary.[13]

DFS oversees the Act's reporting and collateral pledging requirements through its public deposits program and Bureau of Collateral Administration.[14] In addition, the Act gives the CFO authority to take action against noncompliant QPDs, as well as financial institutions that accept public deposits without a certificate of qualification from the CFO. In the event of loss to public depositors, the Act gives the CFO authority to oversee the payment of losses.

Regulation of Credit Unions

Like banks, savings banks, and savings associations, credit unions accept deposits and make loans, and can be state-chartered or federally-chartered:

- *State-chartered credit unions* may be formed under the Florida Credit Union Act (act), which became law in 1980.[15] The act provides that "[a] credit union is a cooperative, nonprofit association, organized . . . for the purposes of encouraging thrift among its members, creating sources of credit at fair and reasonable rates of interest, and providing an opportunity for its members to use and control their resources on a democratic basis in order to improve their economic and social condition."[16] State-chartered credit unions have both a state regulator, the Office of Financial Regulation, and a federal regulator, the National Credit Union Association (NCUA).
- *Federally-chartered credit unions* are chartered under the Federal Credit Union Act of 1934[17] and are regulated by the NCUA.

In addition to regulating both state-chartered and federally-chartered credit unions, the NCUA also operates and manages the National Credit Union Share Insurance Fund (NCUSIF), which insures share (deposit) accounts for members of all federally-chartered credit unions and most state-chartered credit unions.[18] All state-chartered credit unions operating in Florida must carry NCUSIF insurance.[19] The standard maximum share insurance amount is $250,000.[20]

Effect of Proposed Changes

The bill makes state-chartered and federally-chartered credit unions eligible to become QPDs and custodians of pledged collateral.

The bill creates s. 280.042, F.S., to provide criteria that a credit union must meet before the CFO can designate a credit union as a QPD. These provisions are designed to protect public deposits. The credit union is required to submit its agreement of contingent liability and its collateral agreement to the CFO and meet the following requirements:

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[11] s. 280.041(1)(b) and (4), F.S.
[12] s. 280.041(1)(c) and (3), F.S.
[13] s. 280.041(1)(d) and (5), F.S.
[14] *Id.*
[15] Ch. 80-258, Laws of Fla.; codified at ch. 657, F.S.
[16] s. 657.003, F.S.
[17] Public Law 73-467, codified at 12 U.S.C. § 1751 *et seq.*
[18] Federally-chartered credit unions must be insured through NCUSIF, and state-chartered credit unions may be insured through NCUSIF, though some state-chartered credit unions may be insured by private insurance or guaranty corporations. *See* NCUA, *Your Insured Funds*, available at https://www.ncua.gov/Legal/GuidesEtc/GuidesManuals/NCUAYourInsuredFunds.pdf (last visited Mar. 17, 2017).
[19] ss. 657.005(7), 657.008(5)(a)2., and 657.033(9), F.S.
[20] *Id*.

- The credit union must submit a signed statement from a public official of a state or local government indicating that, if the credit union is designated as QPD, the public official intends to deposit more than $250,000 of public funds with the credit union; and
- At least four other credit unions must have each submitted an agreement of contingent liability, a collateral agreement, and a signed statement from a public official of his or her intent to deposit more than $250,000 of public funds with the credit union.

The CFO must withdraw from a collateral agreement previously entered into with a credit union if fewer than five credit unions are designated as QPDs during any period of 90 calendar days or longer. As a result, such a credit union loses its designation as a QPD, and must within 10 days after the CFO's notification of such withdrawal, return all public deposits that the credit union holds to the public official who deposited the funds. Additionally, the CFO may limit the amount of public deposits any one credit union may hold in order to ensure that no single credit union holds an amount of public deposits which may adversely affect the integrity of the program.

In order to prevent credit unions from sharing contingent liability with banks, and vice versa, the bill creates separate mutual responsibility and contingent liability provisions for credit unions. Any credit union that is designated as a QPD and that is not insolvent must guarantee public depositors against loss caused by the default or insolvency of *other credit unions* designated as QPDs. In the event of a default or insolvency of a credit union QPD, any loss to public depositors would be satisfied through any applicable share insurance and then through demanding payment under letters of credit or the sale of collateral pledged or deposited by the defaulting depository. The CFO may assess QPDs, subject to the segregation of contingent liability provided in s. 280.07, F.S., for the total loss if the demand for payment or sale of collateral cannot be accomplished within 7 business days.

The bill requires the CFO to segregate and separately account for any collateral proceeds, assessments, or administrative penalties attributable to a credit union from those attributable to any bank, savings bank, or savings association. Subject to this segregation of funds requirement, the CFO is authorized to pay any losses to public depositors from the Public Deposits Trust Fund.

Lastly, the bill makes conforming changes to allow credit unions to participate in the public deposit program and to subject credit union QPDs to the regulatory oversight of the CFO.

B. SECTION DIRECTORY:

Section 1. Amends s. 280.02, F.S., relating to definitions.

Section 2. Creates s. 280.042, F.S., relating to conditions for designating credit unions as qualified public depositories; withdrawal by the Chief Financial Officer from a collateral agreement and return of deposits; limit on public deposits.

Section 3. Amends s. 280.07, F.S., relating to mutual responsibility and contingent liability.

Section 4. Amends s. 280.08, F.S., relating to procedure for payment of losses.

Section 5. Amends s. 280.09, F.S., relating to Public Deposits Trust Fund.

Section 6. Amends s. 280.03, F.S., relating to public deposits to be secured; prohibitions; exemptions.

Section 7. Amends s. 280.05, F.S., relating to powers and duties of the Chief Financial Officer.

Section 8. Amends s. 280.052, F.S., relating to order of suspension or disqualification; procedures.

Section 9. Amends s. 280.053, F.S., relating to period of suspension or disqualification; obligations during period; reinstatement.

Section 10. Amends s. 280.055, F.S., relating to cease and desist order; corrective order; administrative penalty.

Section 11. Amends s. 280.085, F.S., relating to notice to claimants.

Section 12. Amends s. 280.10, F.S., relating to effect of merger, acquisition, or consolidation; change of name or address.

Section 13. Amends s. 280.13, F.S., relating to eligible collateral.

Section 14. Amends s. 280.17, F.S., relating to requirements for public depositors; notice to public depositors and governmental units; loss of protection.

Sections 15-32. Reenacts various sections of statutes to incorporate amendments to ch. 280, F.S.

Section 33. Provides an effective date of July 1, 2018.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   The bill's impact on state government revenues is indeterminate. However, the potential positive impact to revenues of state government is the same as the potential positive impact to revenues of local governments.

2. Expenditures:

   According to DFS, allowing credit unions to be QPDs will require: [21]

   - Significant programming changes to the Collateral Administration Program ("CAP"), a computer application that tracks account data, monthly and annual report data, and collateral data. CAP also allows accurate administration of any claims for loss from Florida public depositors and potential assessments to QPDs in order to cover public depositor losses. There are several important modules of CAP that must be reprogrammed to provide for the separation of credit union data from data associated with current QPDs (i.e. banks, savings banks, and savings associations).
   - Additional subscriptions to the two nationally recognized financial ranking services, which the public deposits program uses to determine the financial strength or weakness of QPDs and to set collateral requirements.
   - One additional FTE position in order to administer the public deposits program with an increased number of QPDs.

[21] Department of Financial Services, Agency Analysis of 2017 House Bill 1373 (Mar. 23, 2017).

The fiscal impact would be as follows:[22]

	FY 2017-18	FY 2018-19	FY 2019-20
Recurring Expenditures			
Financial ranking services to determine financial condition of a QPD and set collateral requirements	**$5,728**	**$5,728**	**$5,728**
Financial Examiner/Analyst II and annual expenses	$62,388 $10,583	$62,388 $6,317	$62,388 $6,317
Total Recurring Expenditures	**$78,699**	**$74,433**	**$74,433**
Non-Recurring Expenditures Modifications to the Collateral Administration Program, the system used for account management, financial analysis, and collateral administration, to accommodate the addition of credit unions	**$188,650**	**$0**	**$0**

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   The bill's impact on local government revenues is indeterminate. However, a 2014 study by the Office of Program Policy Analysis and Government Accountability explained the potential positive impact to local government public depositors:

   > Federal and state tax differences between credit unions and banks may allow credit unions a competitive advantage when bidding for local government public deposits. Credit unions may also benefit from lower overhead costs since these institutions may use office space belonging to a sponsoring organization. The combined effect of lower taxes and overhead may allow credit unions to pay higher interest rates for public deposits and to provide other business services to local governments at a lower cost than banks.[23]

2. Expenditures:

   None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Allowing credit unions to accept public deposits may generate additional income for the credit unions and provide more options for the public depositors. It is unclear what impact the bill will have on existing QPDs (banks, savings banks, or savings associations). The bill's impact on the private sector is indeterminate due to the number of variables involved in determining such impact.

D. FISCAL COMMENTS:

None.

[22] *Id.*
[23] Office of Program Policy Analysis and Government Accountability, *Issues Related to Credit Unions Operating as Qualified Public Depositories*, Nov. 13, 2014, at 5.

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 action requiring the expenditures of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

DFS has noted that, in order to add credit unions as QPDs, rulemaking is necessary to amend ch. 69C-2, F.A.C., and several forms incorporated by reference in the rules.[24]

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

[24] Department of Financial Services, Agency Analysis of 2017 House Bill 1373 (Mar. 23, 2017).