

Date of Hearing: July 10, 2017

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Matthew Dababneh, Chair

SB 363 (Committee on Insurance, Banking and Financial Institutions) – As Amended May 24, 2017

SENATE VOTE: 36-0

SUBJECT: Financial transactions: corporate entities, securities, loans, and deposits

SUMMARY: Makes changes to the California Finance Lenders Law correcting an unintentional drafting error and enacts changes to provisions of the Government Code regarding deposits.

Specifically, **this bill:**

- 1) Clarifies that the California Finance Lenders Law (CFLL) does not apply to any person who makes *no more than* one commercial loan in a 12-month period (this bill adds the language in italics).
- 2) Authorizes the Trustees of the California State University (CSU) to deposit money in one or more depository institutions located outside the United States, if the amounts on deposit are insured under a foreign law, or if amounts that are not insured under a foreign law do not exceed \$100,000 per depository institution.
- 3) Reduces, from 110% of the amount deposited, to 100% of the amount deposited, the size of a Federal Home Loan Bank (FHLB) letter of credit may be used as security for demand and time deposits made by the State Treasurer.

EXISTING LAW:

- 1) Provides that the CFLL does not apply to any person who makes one commercial loan in a 12-month period (Financial Code Section 22050.5).
- 2) Defines an eligible bank as a state or national bank located in California, selected by the Treasurer for the safekeeping of money belonging to or in the custody of the state, as specified. Provides that an eligible bank is eligible to receive deposits only to the extent that it furnishes security, as specified, but provides that security is not required for any portion of any deposit that is insured under any law of the United States (Government Code Sections 16500 and 16520). Contains a series of requirements applicable to security that is used by an eligible bank to collateralize deposits that are not insured under a law of the United States (Government Code Sections 16521 through 16533).
- 3) Defines eligible savings and loan associations and eligible credit unions in a nearly identical manner as eligible banks, provides that eligible savings and loan associations and eligible credit unions are eligible to receive deposits only to the extent that they furnish security, as specified, but provides that security is not required for any portion of any deposit that is insured under any law of the United States (Government Code Sections 16600 and 16610). Contains a series of requirements applicable to security that is used by an eligible savings

and loan association or eligible credit union to collateralize deposits that are not insured under a law of the United States (Government Code Sections 16601-16622).

- 4) Provides that if a letter of credit from a FHLB is used as security for a state deposit in an eligible bank, the letter of credit must be in an amount equal to at least 110% of the amount deposited with the bank (Government Code Section 16521).

FISCAL EFFECT: According to the Senate Appropriations Committee, pursuant to Senate Rule 28.8, negligible state costs.

COMMENTS: This bill is an omnibus Committee bill for the Senate Committee on Insurance, Banking and Financial Institutions and is intended to enact noncontroversial changes to provisions of law within the jurisdiction of the Committee. The bill makes changes in the following three areas:

- 1) ***De Minimis Exemption for Commercial Loans Under the CFLL:*** Last year, SB 777 (Lara), Chapter 478, Statutes of 2016, re-enacted a de minimis exemption for commercial lending under the CFLL. That bill was supposed to add language to the CFLL stating that that the CFLL does not apply to any person who makes *no more than* one commercial loan in a 12-month period. However, due to an unintentional drafting error, the bill left out the words “no more than.” This bill would add the language that was unintentionally omitted from SB 777, with the aim of clarifying the intent of the exemption.
- 2) ***Authorize CSU to Hold Limited Amounts of Money in Uninsured Foreign Banks:*** Existing law authorizes state funds to be placed with eligible depository institutions, as long as those deposits are insured or are backed with adequate collateral, the rules for which are specified in state law.

CSU maintains relatively small amounts of money (under \$100,000) in bank accounts in certain foreign countries in which it runs foreign exchange programs. This money is used to cover operational expenses such as stipends for local coordinator positions, transportation costs for students, material fees, and museum tickets. According to CSU, extensive efforts have been undertaken to find foreign banks that can comply with the requirements of the Government Code, but those efforts have proven unsuccessful.

This bill would amend the Government Code to allow CSU to maintain depository accounts in foreign countries. Amounts held on deposit in foreign depositories would either need to be insured under a foreign law or, if uninsured, would need to total less than \$100,000 per depository institution.

- 3) ***Reduce the Collateral Requirement for Letters of Credit Provided by Federal Home Loan Banks:*** In 2015, the Government Code was amended at the State Treasurer’s request, to allow state depository banks headquartered outside of California to submit letters of credit from their regional FHLBs as security for state demand deposits. Prior to that amendment, the statute limited letters of credit used to secure state deposits to those issued by the FHLB of San Francisco, which limited the ability of banks headquartered outside of California to use FHLB letters of credit as collateral. Since the statute was amended, a number of the state’s larger depositories have begun relying heavily on FHLB letters of credit as security for deposits held at their banks.

According to the Treasurer's Office, FHLB letters of credit have high credit quality, maintain face values that do not fluctuate with the market; can be paid quickly and directly to beneficiaries on presentment; and are not subject to call provisions. Many public entities prefer letters of credit to direct issue securities, because the value of the former does not fluctuate with the market, while the value of the latter may.

Under existing law (Government Code Section 16521), FHLB letters of credit must be pledged at 110% of the amount on deposit, similar to other types of securities. The State Treasurer's Office is seeking to lower this requirement to 100%, on grounds that the current requirement is unnecessary and adds needless cost to the state's banking partners. Not only do letters of credit hold their value, but if a bank in which the state had a deposit backed by a FHLB letter of credit failed, the state would receive only the amount deposited, not 110% of that amount. The 110% requirement adds no value to the state, while imposing higher costs on the banks in which the state deposits money.

REGISTERED SUPPORT / OPPOSITION:**Support**

California Bankers Association
California Community Banking Network
California State University, Office of the Chancellor

Opposition

None on file

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