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SFA BILL ANALYSIS

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Senate Bill 745 (as enrolled) **PUBLIC ACT 276 of 1999**
Sponsor: Senator Joanne G. Emmons
Senate Committee: Banking and Financial Institutions
House Committee: Insurance and Financial Services

Date Completed: 1-18-00

RATIONALE

While there have been numerous amendments to the Banking Code of 1969 in the past 30 years, there have been many more changes to the banking industry. When enacted, the Code was designed to regulate an industry that is much different today. In 1969, banks were protected from competition and heavily regulated; there were no electronic transfers of assets and no electronic data storage; and bank auditors conducted audits on-site by counting money by hand. In the ensuing years many bank products have been modernized, the number and type of products offered have increased, and the delivery of services has been altered substantially. Regulations on banks have been relaxed and reduced, the Federal government deregulated much of the industry in the 1980s, interest rates have been deregulated, and bank branching has been expanded greatly. Banks now face competition from out-of-region and out-of-state banks that previously were forbidden from opening in another bank's territory; and from other industries (insurers, mutual funds, mortgage companies, etc.) that now offer consumers products that once were available primarily from banks. It was suggested that the Code should be updated to reflect the changes that have occurred, and to ensure proper regulation of the industry in the future.

CONTENT

The bill repeals and recodifies the Banking Code of 1969. The bill establishes the "Banking Code of 1999" to provide for the regulation of banks; prescribe their powers and duties; provide for bank structure and organization, and banking operations; and prescribe the powers and duties of the Financial Institutions Bureau (FIB) and its Commissioner in the regulation of banks. The bill will take effect March 1, 2000.

Bank Operations

The bill revises and recodifies provisions regarding the issuance of bank stock. Among other things, the bill regulates the division of stocks into classes and series; requires that a bank keep and maintain accurate records of shareholders' identities and submit that information to the Commissioner upon demand; requires that certificates of stock be issued to every shareholder and transferable on the bank's books; allows a bank's directors to sell a shareholder's shares, 30 days after the shareholder refuses or neglects to pay an assessment levied on the shares, and establishes a list of priorities for distribution of the proceeds of the stock sale; provides that a bank's assessment and sale of a shareholder's stock is limited by provisions in the Uniform Commercial Code; allows preferred shareholders, by unanimous vote, to waive their right to unpaid dividends; and requires that dividends be paid from net income (rather than net profits, as is currently required).

The bill also does the following:

-- Requires every bank employee who handles money, accounts, or securities to be bonded. (Currently, the bonding requirement is for those employees "who can be bonded".)
-- Requires every bank to maintain a financial institutions bond sufficient to protect against loss.
-- Limits all indemnification expenses of a bank to "actual and reasonable" expenses incurred by a director, officer, employee, or agent of the bank who is a party to a lawsuit or proceeding.
-- Allows a bank's board of directors to be elected with staggered terms of office. (This is not allowed under the current Code.)
-- Allows a board of directors to meet in person or by electronic communication devices, rather than only in person. (The bill continues to require a board to meet six times per year.)
-- Allows the board of directors to appoint committees of its members to perform its

duties; and requires the board to appoint a member, who is a full-time employee of the bank, to be chief executive officer to perform duties designated by the board.

-- Specifies that a bank may purchase or sell securities or other property from or to its directors, in the ordinary course of business, if the terms of the transaction are not more favorable than those offered to others and the transaction is authorized by a majority of the bank's directors.
-- Prohibits a bank officer, director, or employee from receiving or agreeing to receive from a customer any gratuity or consideration in return for the procurement of a loan or other bank service.

<u>Bank Organization and Structure</u>

The bill does the following:

-- Specifies that a bank holding company may file an application to organize a bank. (Currently, only natural persons may incorporate to organize a bank.)
-- Provides that, after authorization by the Commissioner to commence business, a bank and its incorporators may request permission from the Commissioner for the bank to reimburse the incorporators for reasonable and necessary organizational expenses. The request must include an accounting of the funds spent by the incorporators, as prepared by an independent certified public accountant. The Commissioner may waive the requirements if the expenses of organization will be paid by a bank holding company.
-- Specifies that after an approval of a bank application, two articles of incorporation must be submitted to the Commissioner, one to be retained by the FIB and one to be forwarded to the incorporators. (Currently, four articles must be submitted, including one that is forwarded to the Department of Treasury and one to the county clerk of the county where the bank is located.)
-- Prescribes the procedures for submitting applications to the Commissioner for various required approvals under the bill, including approval to establish a bank or consolidate banks. An application will be accepted when it is considered by FIB to be complete; after acceptance the applicant may amend the application. The Commissioner must approve or disapprove an application within 100 days after acceptance; an applicant may not appeal that decision until the applicant has requested a reconsideration of the application.
-- Provides that a bank may be converted to a stock association, stock savings bank, or national banking association, upon the affirmative vote of shareholders who represent over 50% of total shares. (Currently, a two-thirds majority is required.)
-- Provides that a national banking association, stock association, or stock savings bank may be converted into a bank, upon the affirmative vote of shareholders who represent over 50% of total shares. (Currently, a two-thirds majority is required.)
-- Reduces to 30 days (from 60 days) the opportunity for the Commissioner to object, in writing, to the establishment of a branch by a bank.
-- Allows a national bank located in another state to establish and operate one or more branches in Michigan.
-- Allows a bank to change the location of its principal office to any existing branch location within the State, with prior written notice to the Commissioner. (Currently, a bank must obtain the written approval of the Commissioner to change the location of its principal office.)

The bill also retains current provisions that require any consolidating organizations that propose to form a consolidated bank to hold a separate meeting of the shareholders of each organization. While the bill requires that a notice of the meeting be mailed to each shareholder, as is currently required, the bill does not retain the current requirement that notice of the meeting be published once a week for the four weeks prior to the meeting. Notice will not be required if it is waived by the Commissioner; notice to an individual shareholder will not be required if the shareholder waives the notification requirement. A consolidated bank or organization may operate all branches and principal offices of the consolidating organizations without further notice to the Commissioner.

<u>Bank Powers</u>

The bill does the following:

-- Specifies that banks may engage in any aspect of the insurance and surety business. (Currently, the Code forbids the Commissioner from authorizing banks to engage in an insurance business; however, banks are allowed to sell insurance as provided in the Insurance Code.)
-- Specifies that banks have powers granted by order or declaratory ruling of the Commissioner.
-- Revises and rewrites the specific list of

powers banks have and may exercise.

-- Revises and rewrites procedures that must be followed regarding the voluntary dissolution of a bank, including provisions specifying the duties and responsibilities of a liquidator, the shareholders, the bank, the directors, and the Commissioner.
-- Allows any number of depository institutions to organize a "bankers' bank", exclusively to serve the institutions and their officers and affiliates, that may provide trust services or other services authorized by the Commissioner, and requires that the "bankers' bank" stock be owned by the member institutions.
-- Allows a bank to sell one or more of its branches, or purchase a branch or branches from another institution. A bank must notify the Commissioner before it operates a purchased branch.
-- Specifies that all mortgages or other securities held by banks are exempt from all municipal or other taxes under State law; and that all personal property owned by banks is exempt from taxation.

<u>FIB Operations and Commissioner Powers</u>

The bill does the following:

-- Requires each bank and its subsidiaries to be examined by the Commissioner or an authorized agent at least once every 18 months. (Currently, an examination must be conducted at least once per year.) The bill specifies that the Commissioner may make an examination of a bank holding company.
-- Specifies that the contents of an examination report will remain the property of the FIB; and dissemination of all or part of a bank's examination for purposes other than the legitimate business purposes of the bank is a violation of the bill, subject to administrative remedies granted to the Commissioner.
-- Recodifies current annual bank supervisory fees, but eliminates a provision that requires a refund of the fee for those banks that are not examined during the year.
-- Allows the Commissioner to promulgate rules, rather than requiring promulgation as is currently prescribed.
-- Allows the Commissioner by order or declaratory ruling to exceed the loan limit of a bank. (Currently, and as provided in the bill, the total loans and extensions of credit by a bank to a person at no time may exceed 15% of the bank's capital and surplus.)
-- Allows the Commissioner, by order or declaratory ruling, to authorize a bank to invest in assets other than those specifically allowed under the bill.

In addition, the bill prohibits the Commissioner from accepting employment with a State-chartered depository financial institution, for six months from the date he or she leaves office.

<u>General Provisions</u>

The bill does not include references to industrial banks or to trust companies. (Under the current Code, the distinction between banks and industrial banks or trust companies was abolished with the effective date of the Code (August 20, 1969), and neither industrial banks nor trust companies could be created after that date, though existing entities could continue.)

The bill does not include a provision in the current Code that requires FIB employees to be bonded.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill modernizes and reorganizes the State's 30-year-old Banking Code to allow both banks and bank regulators to deal with the changes that have occurred in the industry, and provides increased flexibility for banks and the State's regulators to respond to the industry as it evolves in the future. The bill removes obsolete provisions, recognizes new technologies and the State's role in supervising their use, and acknowledges changes in the marketplace in which banks and bankers conduct business. For example, the bill allows a board of directors to meet in person or by electronic communication devices; prescribes the procedures for submitting applications to the Commissioner for various required approvals, including approval to establish or consolidate banks; specifies that banks may engage in any aspect of the insurance and surety business; specifies that banks have powers granted by order or declaratory ruling of the Commissioner, and allows the Commissioner, by order or declaratory ruling, to authorize a bank to invest in assets other than those specifically allowed under the bill; allows any number of depository institutions to organize a "bankers' bank", exclusively to serve the institutions and their officers and affiliates; and requires each bank and its subsidiaries to be examined by the Commissioner or an authorized agent at least once every 18 months (rather than at least once a year). These changes, and many others, maintain necessary regulations on banks and allow the FIB to perform its responsibilities efficiently.

Opposing Argument

Under the bill, the FIB Commissioner is prohibited from accepting employment with a State-chartered depository financial institution for at least six months from the date of his or her resignation. To safeguard against conflicts of interest by the State's chief banking regulator, the time limit should be increased substantially.

Response: On the contrary, this provision should be deleted entirely. The State benefits enormously from the willingness of people with practical banking experience to interrupt their careers, sometimes at considerable financial sacrifice, to serve as regulators. Denying these people the opportunity to return to their careers is unfair, and discourages talented people from considering State service.

Legislative Analyst: G. Towne

FISCAL IMPACT

The bill will have no fiscal impact on State or local government.

Fiscal Analyst: M. Tyszkiewicz