



Senate Fiscal Agency  
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## BILL ANALYSIS



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Senate Bills 748, 749, and 750 (as enacted)  
Sponsor: Senator Darwin L. Booher (S.B. 748)  
Senator Dale W. Zorn (S.B. 749)  
Senator Mike Nofs (S.B. 750)  
Senate Committee: Banking and Financial Institutions  
House Committee: Financial Services

**PUBLIC ACTS 175-177 of 2016**

Date Completed: 1-12-17

**CONTENT****Senate Bill 748 amended the Banking Code to do the following:**

- Establish the "State Bank Union Regulatory Fund", and specify the disposition of fees, expenses, compensation, penalties, and appropriations to the Fund.
- Specify that if an institution under the jurisdiction of the Director of the Department of Insurance and Financial Services (DIFS) engages a service provider to perform services, the performance is subject to regulation, examination, and enforcement by the Director.
- Specify that contents of a report of an examination of a bank and examination-related documents and materials are the property of the Director, are confidential and privileged, are not subject to the Freedom of Information Act or subpoena, and are not subject to discovery in any private civil action.
- Prohibit the Director from testifying, or being compelled to testify, in any private civil action concerning any confidential documents or materials.
- Allow the Director to share and receive documents or materials from other regulatory agencies, and enter into agreements covering the sharing and use of information.
- Require any request for discovery or disclosure of confidential and privileged documents or materials to be made to the Director, and require the Director to determine within 21 days whether to disclose the information.
- Specify that the Director's refusal to disclose confidential information is subject to judicial review, including in camera review of the documents or materials.
- Allow the Director to suggest best practices or other improvements in the operation of a bank in an addendum to a report of examination.
- Require the Director to issue guidance pertaining to the bank examinations.
- Modify the annual supervisory fee to be paid by banks.
- Allow the Director to suspend a person from office or prohibit the person from further participation in the affairs of an institution if the person is charged with a misdemeanor involving fraud, dishonesty, or breach of trust.
- Allow a bank to pledge its assets to counterparties to secure their exposure in interest rate swap transactions.

**Senate Bill 749** amended the Banking Code to modify the definition of "affiliate" and add a definition of "derivative transaction".

**Senate Bill 750** amended the Banking Code to do the following:

- **Specify that the statutory limit on the amount of investment securities of any one obligor or maker that may be held by a bank is determined by generally accepted accounting principles, instead of the par or face value of the securities.**
- **Allow the DIFS Director to require a bank to develop a plan for the divestiture of an investment that at the time of the investment was permitted, but later becomes impermissible.**

Each bill took effect on September 12, 2016.

### **Senate Bill 748**

#### **State Bank Union Regulatory Fund**

Previously, the fees, expenses, compensation, penalties, and fines collected under the Banking Code had to be paid into the State Treasury to the credit of the Department of Insurance and Financial Services, for its operations. The bill eliminated this requirement.

The bill established the State Bank Union Regulatory Fund in the Department of Treasury. The Fund must consist of the following:

- Fees, expenses, compensation, penalties, and fines received or collected under the Code.
- Money appropriated to the Fund.
- Donations of money made to the Fund from any source.
- Interest and earnings from Fund investments.

Upon appropriation, the Department of Financial and Insurance Services must use the money in the Fund only for bank regulatory purposes, as determined by the Director. The State Treasurer is required to direct the investment of the Fund, and DIFS is the administrator for auditing purposes. Money in the Fund at the close of a fiscal year must remain in the Fund and may not revert to the General Fund.

#### **Examination of Financial Institution & Associated Entities**

The Code specifies that each institution, and its subsidiaries and service entities, is subject to examination of its condition and affairs by the Director or his or her authorized agent at least once every 18 months. In addition, the Director must examine an institution under his or her jurisdiction when requested by its board of directors. The Director must ascertain whether the institution transacts its business in the manner prescribed by law and applicable rules. Formerly, the Director also could examine an affiliate, bank holding company, subsidiary, or service entity as necessary to disclose the relation between an institution and the entity, and the effect of the relation on the institution.

Under the bill, if an institution under the Director's jurisdiction engages a service provider to perform any services of a service provider, whether on or off its premises, that performance is subject to regulation, examination, and enforcement by the Director to the same extent as if those services were performed by the institution itself on its own premises. The Director may examine an affiliate or bank holding company of an institution under the Director's jurisdiction.

The bill defines "service provider" as a person that provides any of the following to an institution: a) data processing services; b) activities that support financial services, including lending, fund transfer, fiduciary activities, trading activities, and deposit taking; c) internet-related services, including web services and electronic bill payments, mobile applications, systems and software development and maintenance, and security monitoring; or d) activities related to the business of banking.

## Bank Examination Report

Under the Code, the contents of a bank examination report and related documents remain the property of DIFS. Formerly, dissemination of all or part of the report for purposes other than the bank's legitimate business purposes or as otherwise authorized under the Code was a violation of the Code subject to administrative remedies.

Under the bill, any document, material, or information related to an examination under the Code is confidential by law and privileged, is not subject to the Freedom of Information Act, subpoena, or discovery, and is not admissible in evidence in any private civil action. However, the Director is authorized to use the documents, materials, or information in furtherance of any supervisory activity or legal action brought as part of the Director's duties. The Director, or any person that receives documents, materials, or information while acting under the Director's authority, is not permitted and may not be required to testify in any private civil action concerning any confidential documents, materials, or information related to an examination.

Under the bill, to assist in the performance of his or her duties under the Code, the Director may share documents, materials, or information with other State, Federal, and international regulatory agencies and law enforcement agencies, provided that the recipient agrees to maintain the confidentiality and privileged status of the documents, materials, or information. The Director may receive documents, materials, or information from regulatory and law enforcement officials of foreign or domestic jurisdictions. The Director must maintain as confidential or privileged any document, material, or information received with notice or the understanding that it is confidential or privileged under the laws of the source jurisdiction. The Director also may enter into agreements governing the sharing and use of the documents, materials, or information.

The bill provides that the disclosure of any documents, materials, or information to the Director, or the sharing of the documents, materials, or information is not a waiver of, and may not be construed as a waiver of, any privilege applicable to or claim of confidentiality in them. A person to which a confidential and privileged document, material, or information is disclosed may not further disseminate it. Any person to which a demand for production of a confidential and privileged document, material, or information is made, whether by subpoena, order, or other judicial or administrative process, must withhold production of it and notify the Director of the demand. If the Director is notified of a demand, he or she may intervene to enforce the bill's limitations or to seek withdrawal or termination of the attempt to compel production.

The bill requires any request for discovery or disclosure of a confidential and privileged document, material, or information to be made to the Director, who must determine within 21 days whether to disclose it. If the Director determines that the document, material, or information will not be disclosed, his or her decision will be subject to judicial review. Judicial review may include in camera review (a review not open to the public) of the document, material, or information. After review, a court may order disclosure only of the portions of the document, material, or information that are relevant and otherwise unobtainable by the requesting party. The Director may immediately appeal any court order that compels disclosure of a confidential and privileged document, material, or information, and the order will be automatically stayed pending the outcome of the appeal.

The bill also allows the Director or his or her authorized agent, in an addendum to a report of an examination, to suggest best practices or other improvements in the operation of a bank that are not required by law or regulation or to address safety and soundness of the bank. The manner in which a bank addresses issues concerning its operations will be within the discretion of the bank in the exercise of its business judgment, except as required by law or

regulation or to address a concern over safety and soundness. The Director may not take action against a bank under the Code based on its failure or refusal to follow a best practice or recommended improvement that is suggested informally by an examiner or that is contained in an addendum.

Within one year of the bill's effective date, the Director must issue guidance to promote consistency and due process in the examination process, including establishing guidelines that define the scope of the process and clarify how examination issues will be resolved.

#### Annual Supervisory Fee

The Code requires the Director to establish a schedule of supervisory fees to be paid by banks. Previously, except for a minimum fee of \$1,000, the fee could not be more than 25 cents for each \$1,000 of total assets of the bank as reported by it on its report of conditions as of December 31 of the previous year. Under the bill, the annual supervisory fee to be paid by banks may not exceed 1/40 of 1% of the total assets of the bank as reported by it in 2016, 1/20 of 1% in 2017, 3/40 of 1% in 2018 and 2019, and 1/10 of 1% in 2020 and in subsequent years. The minimum fee remains \$1,000.

#### Order of Removal, Prohibition

Under the Code, if a person that participates in an institution's affairs is charged in any information, indictment, warrant, or complaint by a county, State, or Federal authority with the commission of, or participation in, a felony that involves fraud, dishonesty, or breach of trust, the Director, by written notice served upon the person, may suspend him or her from office or prohibit the person from further participation in the conduct of the affairs of the institution. The bill includes misdemeanors satisfying the same criteria.

#### Pledging Bank Assets & Bank Investment Authority

Generally, the Code prohibits a bank or bank officer from giving preference to a depositor or creditor by pledging the bank's assets as collateral security or otherwise. The bill allows a bank to pledge its assets to counterparties to secure their exposure in interest rate swap transactions.

The Code permits a bank to purchase and hold shares of stock or other equity interests, that have an aggregate purchase price that is not more than 10% of its capital and surplus, of certain businesses and other entities enumerated in the Code. Subject to this limitation, a bank may purchase for its own account certain other investments. Under the bill, these include stocks, bonds, or other obligations or community and economic development entities, community development projects, and other public welfare investments that are considered under Federal law, Federal regulation, or a written interpretation by a Federal bank regulator agency to be a qualified investment for purposes of the Community Reinvestment Act, using the investment test described in 12 CFR 25.23, 12 CFR 228.23, or 12 CFR 345.23.

(Those Federal regulations prescribe substantially similar tests to evaluate a bank's record of meeting the credit needs of its assessment areas (designated geographical areas) through qualified investments.)

### **Senate Bill 749**

The bill defines "affiliate" as a corporation, business trust, limited liability company, partnership, association, or similar organization to which any of the following apply:

- A person owns or controls either more than 25% of its voting shares or a majority of the shares voted at the most recent election for its directors, trustees, or other individuals

who exercise similar functions, or controls in any manner the election of a majority of its directors, trustees, or other individuals who exercise similar functions.

- Control of the organization is held through one of the following: a) stock ownership or in any other manner, by the shareholders or members of an organization that own or control more than 25% of the shares of or the ownership interest in the organization, a majority of the shares voted for the election of directors at the most recent election, or a majority of the ownership vote for election of directors at the most recent election; b) by trustees for the benefit of the shareholders or members of the organization; or c) by the power to exercise a controlling influence over the management of policies of the organization, as determined by the Director after notice and an opportunity for a hearing.
- A majority of its directors, trustees, or other individuals who exercise similar functions constitutes a majority of the directors, trustees, or other individuals who exercise similar functions of any of any one organization.
- The organization owns or controls either more than 25% of the shares of capital stock or other ownership interest or an organization, or a majority of the shares voted of the total ownership vote for directors of an organization at the preceding election, or controls in any manner the election of a majority of the directors of an organization, or for the benefit of whose shareholders or members all or substantially all of the capital stock of ownership interest of an organization is held by trustees.

Previously, the definition referred to ownership or control of either a majority of an organization's voting shares (or shares of an organization, or shares of capital stock or other ownership interest, as applicable) or more than 50% of the number of shares voted for its directors, trustees, or other persons exercising similar functions (or for directors). In addition, in the second portion of the definition, it previously did not include part "c)".

The bill defines "derivative transaction" as any transaction that is a contract, agreement, swap, warrant, note, or option that is based, in whole or in part, on the value of, any interest in, or any quantitative measure or the occurrence of any event relating to, one or more commodities, securities, currencies, interest or other rates, indices, or other assets.

### **Senate Bill 750**

The Code limits the amount of investment securities of any one obligor or maker that a bank may hold. That limitation formerly was determined on the basis of the par or face value of the securities. The bill specifies that the statutory limitation on the amount of investment securities of any one obligor or maker that may be held by a bank is determined on the basis of generally accepted accounting principles unless otherwise directed or permitted in writing by the Director for safety and soundness reasons.

The bill also provides that if a bank invests money in a security, obligation, or other instrument that at the time is permitted under the Code, the investment subsequently becomes impermissible because of a change in circumstances or law, and the Director finds that continuing to hold the investment will have an adverse effect on the safety and soundness of the bank, the Director may require the bank to develop a reasonable plan for the divestiture of the investment.

MCL 487.11202 et al. (S.B. 748)  
487.11201 (S.B. 749)  
487.14301 (S.B. 750)

Legislative Analyst: Jeff Mann

## **FISCAL IMPACT**

### **Senate Bill 748**

The bill will result in increased administrative burdens for the Department of Insurance and Financial Services and Department of Treasury related to the establishment of the State Bank Union Regulatory Fund.

### **Senate Bills 749 and 750**

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

Fiscal Analyst: Michael Siracuse

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.