

Office of the Washington State Treasurer

2009 Report to the Washington State Legislature on Actions Taken by the Public Deposit Protection Commission

An update on recent events, responses, rulemaking and issues
related to modernizing and improving the protection of public
deposits in Washington State

December, 2009

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Introduction:

The 2009 Legislature unanimously passed Substitute House Bill 2061 to address systemic risks to state and local government public deposits and financial institutions that came to light during the financial collapse of 2007-2009. The measure provides greater discretion to the Public Deposit Protection Commission (PDPC) and additional authority to the State Treasurer. It facilitates the efficient and effective implementation of new reporting, rulemaking and administrative requirements for banks, savings banks, and savings associations. With this additional authority and agility the PDPC and Treasurer can respond to rapid changes in both the economy and the condition of financial institutions.

On March 6, 2009, Gov. Chris Gregoire signed SHB2061 and it took effect immediately. The PDPC and the Treasurer then acted quickly to reduce the risk that an individual bank failure would jeopardize public tax dollars and the broader network of financial institutions authorized to accept public deposits.

The new law requires the State Treasurer to provide an annual report to the Legislature on actions taken by the Commission and the State Treasurer regarding public deposit protection.

In compliance, this report is intended to provide an accounting of the issues and actions taken by the Public Deposit Protection Commission and the State Treasurer to protect public deposits. It also summarizes the outcomes and emerging issues as of August 23, 2009, the date new, updated rules and procedures took effect for financial institutions that hold public funds.

Executive Summary:

On January 16, 2009, a failed bank holding more than \$15 million in uninsured and uncollateralized public deposits triggered a first-ever assessment on other public depositaries to recover public funds that would otherwise have been lost. The 40-year-old Public Deposit Protection Act served its purpose and provided the necessary guidelines to recover the public tax-dollars lost in the closure but not without causing hardships for financial institutions. The unfortunate event also drove home the need for reform. Inaction would have jeopardized \$8 billion in public deposits and the state's financial institutions.

Swift and prudent action by the Legislature, Governor, the State Treasurer and regulators has reigned in the systemic risk to public deposits and the financial system. The Office of the State Treasurer is pleased to report that as of June 30, 2009, public deposits that previously could have been lost are now either fully insured or fully collateralized. By working together, we have created better protections for public deposits while also reducing risks and liabilities for financial institutions.

We have come a long way since the Bank of Clark County's failure. Having 100 percent collateral standing behind uninsured public deposits has already reduced risks and liabilities. The FDIC closed three other banks this year: Westsound, Venture and United Commercial Bank. In each case, the acquiring institution agreed to purchase the bank that was closed by regulators in a way that protected public deposits and prevented additional assessments.

Our 105 public depositaries now hold more than \$8 billion in public funds that are either fully insured or fully collateralized. The 100 percent collateral level for uninsured public funds was attainable in part because FDIC insurance coverage for qualifying non-interest bearing accounts is available through the Transaction Account Guarantee (TAG) program. The

enhanced coverage allows financial institutions to accept large public deposits in accounts that do not require collateral.

As of mid July 2009, more than half of the \$8.2 billion in public deposits was in fully insured accounts. The TAG program provides added liquidity and stability for financial institutions and local governments benefit by continued service from the banks they rely on. Perhaps most important, public confidence in financial institutions and the economy is bolstered at what is still a fragile time.

The federal TAG program was originally scheduled to sunset December 31, 2009 but the State Treasurer marshaled forces from among a broad range of stakeholders nationwide to successfully advocate for an extension of this program through June 30, 2010.

As a result, a significant amount of public deposits will continue to be federally insured through what is anticipated to be the worst part of this current economic crisis.

Although some public depositories in Washington still face significant challenges the actions of the Legislature, Governor, the Public Deposit Protection Commission, local government finance officers and financial institutions has eliminated the untenable risks that were allowed under the previous statute.

Background:

In 1969, Washington State changed its public deposit protection laws and set the framework for the system in place today.

Previously, state laws required individual banks to bear the responsibility of insuring public deposits. Each bank was required to execute a collateral agreement with the public treasurer with a deposit account. To guarantee against loss, the bank was required to place securities in escrow valued at 110% of each public treasurer's bank account balance.

In contrast, the 1969 laws allowed financial institutions to draw on the collective strength of the participating depositaries by creating a collateral pool. Though not an actual collateral account, banks authorized to accept public tax-dollar deposits from state and local governments assumed proportional liability for all public deposits. In addition, the Public Deposit Protection Act (the "Act") lowered the collateral requirement for individual banks to 5 percent. In 1977 the Legislature increased the collateral requirement to 10 percent.

In the event a public depositary fails, the other authorized institutions are responsible for providing funds to cover public deposits that are either uninsured or not collateralized, on a pro-rata basis.

Financial institutions benefitted greatly from additional liquidity made possible by substantially reduced collateral requirements that did not require increased insurance premiums. The public benefited from increased convenience and ability for governments to safely deposit public funds in local banks.

For 40 years, the Act remained untested because no banks were closed in ways that could have resulted in lost public deposits. Because it appeared to be functioning, the Act was amended only occasionally with changes aimed generally at reducing restrictions or expanding participation. For example, in 1983, the Act was amended to allow savings banks and savings and loan associations to become public depositaries. A separate collateral pool was created for these new participants.

Signs of trouble:

Relative stability in the banking industry over four decades preserved the Public Deposit Protection Act in essentially its original form, but that stability was shaken by the financial crisis of 2008. As venerable financial institutions foundered, it became clear the status quo could no longer adequately protect public deposits.

On September 25, 2008, Washington Mutual Bank (WaMu) became the largest bank failure in U.S. history. It should have been a wake-up call. Washington State narrowly averted a much larger disaster that could have crippled all 11 other public depositary savings and loans and could have resulted in the loss of as much as \$727 million in public funds.

When JPMorgan Chase bought Washington Mutual, it agreed to honor the uninsured public deposits held by WaMu. Washington narrowly avoided a situation that would have required a problematic assessment on the state's much smaller remaining public deposit savings and loans. Had JP Morgan taken only the insured deposits, the Public Deposit Protection Commission would have been required to assess the 11-member thrift pool \$51.3 million to cover uninsured public fund losses. This estimate is based on a 10 percent maximum liability associated with the June 2008 quarterly reports from the remaining 11 pool participants.

When federal regulators took control of WaMu on September 28, it was holding between \$440 million and \$872 million public deposits with only \$93.8 million in pledged collateral. Combined, the funds that would have been collected from the thrift pool and the collateral available from the bank would have been insufficient to cover the losses. As much as \$727 million in public funds could have been lost.

These events were a clear warning that the outdated Public Deposit Protection Act had created an unacceptable risk to public tax dollars and financial institutions. However, at that time no action plan or risk assessment was prepared nor was legislation offered to update the Public Deposit Protection Act.

The First Bank Assessment in 40 years:

Three days after the new Treasurer's administration took office the risks to public deposits and to financial institutions became reality.

On January 16, 2009, the Washington Department of Financial Institutions (DFI) closed the Bank of Clark County and immediately appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. In turn, the FDIC sold the bank's insured deposit accounts and fixed assets (which excluded loans and investments). Most of the bank's operations resumed -- under new ownership -- on the first business day of the following week.

Under the terms of the sale negotiated by the FDIC, the acquiring institution was not required to honor the uninsured portion of public deposits. In Washington, uninsured public deposits are backed by a collateral pool from depositaries. However, at that time, public depositaries in Washington, including Bank of Clark County, were required to have only 10 percent collateral for their public deposits.

Several public entities had a total of \$23.9 million deposited with Bank of Clark County when it was closed on January 16, 2009. The FDIC - working with the DFI and the State Treasurer's Office - applied federal deposit insurance and the collateral designated by the Bank of Clark County to leave \$15.1 million in unsecured deposits belonging to four local government entities: Clark County, the City of Ridgefield, the Port of Ridgefield, and the City of Vancouver. All other public deposits were covered by actions taken by the FDIC.

State law (RCW 39.58.060) provides that public depositaries are assessed on a pro rata basis for the share of public funds each has on deposit in their bank. Once the assessment is levied each bank must remit its share of the total amount of the loss to the State Treasurer's Office within 48 hours or the bank's collateral will be redeemed to cover their payment.

As required under the Public Deposit Protection Act of 1969, the members of the pool were assessed to cover the \$15 million of unsecured public deposits and all public deposits were made whole within 30 days.

Viewed in conjunction with the meltdown at Washington Mutual, it was clear that immediate action was necessary.

Role of the Washington State Treasurer's Office:

The Washington State Treasurer's Office implements the laws, rules and procedures related to the work of the PDPC, established by the Legislature in 1969 to ensure that state and local government funds deposited in state and federally chartered banks are not lost should a bank fail.

In such an event, state law compels both the PDPC and the state's public depositaries to act in a timely manner to restore public funds to the depositors. The law requires that the PDPC levy a pro rata assessment on each of the remaining banks acting as public depositaries. The assessed amounts are sent to depositaries by the State Treasurer.

In the case of an assessment, payments remitted to the State Treasurer's Office are apportioned among the public entities to cover remaining deposits that were not insured or covered by the assets of the Bank.

Early Response:

As required by statute, the State Treasurer administered the assessment of the public depositary banks that make up Washington's collateral pool and restored the unsecured local government deposits that had been held in Bank of Clark County.

The first step of our response was to establish a better working relationship with the Washington State Department of Financial Institutions leadership and staff. Recognizing the clear public interest and need for sharing information about the health of financial institutions, our agencies agreed to a memorandum of understanding (MOU) that made it possible for us to quickly improve risk assessment processes and implement responses in a rapidly changing environment.

In addition, the Treasurer initiated a statewide outreach to county treasurers and other stakeholders to communicate the facts about the situation and identify issues of concern as new rules were developed.

The Treasurer also sought input from the Legislature and worked cooperatively with lawmakers to expeditiously put the needed statutory changes in place.

Simultaneously, the Treasurer set in motion a system-wide update of the rules and responsibilities for commercial bank and thrift public depositaries.

The Treasurer's first and foremost responsibility is to ensure the protection of all public funds. That objective was achieved without threatening the viability of any of Washington's financial institutions.

The Office of the State Treasurer provided staff briefings for the two other members of the Public Deposit Protection Commission, Gov. Christine Gregoire and Lt. Gov. Brad Owen. The Commission reviewed the issues and recommended rulemaking changes.

Working with financial institutions and local government representatives, the PDPC set new collateral requirements for all public depositaries to be implemented by a June 30, 2009. In addition, the PDPC requested additional information from banks and thrifts in the form of enhanced monthly reporting of deposits, securities pledged, net worth, loans and assets.

For the financial institutions that were the most challenged, PDPC requested semi-monthly reporting.

In an effort to make the transitions without undue strain on the banks and thrifts, the Treasurer encouraged county treasurers, other local government financial officers and banks to

utilize new federal deposit insurance coverage where ever possible. By shifting some public deposits into non-interest bearing accounts, local governments were able to reduce the burden of collateralization and increase liquidity for the banks in their communities.

Resolution No. 2009-1 set July 1, 2009 target for all banks and thrifts that operate as public depositaries to collateralize their uninsured public deposits at 100 percent (copy attached). This important step was intended to increase the Commission's capacity to better protect public deposits and reduce the likelihood for additional assessments should more public depositaries fail.

Legislation:

At the requests of the Commission, lawmakers in both chambers held hearings on the proposed changes to the Public Deposit Protection Act. Identical versions of the final bill passed in House and Senate committees. Since the House version was first to receive a full floor vote, the Senate advanced its legislation by substituting the House bill with a unanimous vote.

To facilitate the immediate actions necessary to protect public deposits and financial institutions House Bill 2061(see appendix) clearly defined the Public Deposit Protection Commission's authority as well as the rules for Public Depositaries. The updated statute is summarized in the attached final bill report.

New Powers of the Commission:

The Commission is given "broad administrative discretion" in performing its general powers.

The Commission may delegate all of its authority to the State Treasurer, except rulemaking. The enforcement authority of the Commission is clarified.

The Commission may assess costs or deny, suspend, or revoke authority to hold public funds, if a public depositary fails to: provide, or allow verification of, required information; or comply with relevant laws and rules or policies of the Commission.

The Commission may make and enforce sanctions against a public depositary for noncompliance with relevant laws, rules, or policies.

The Commission is authorized to set by resolution, based on criteria established in rule, a sum or measure as the maximum liability of public depositaries. The State Treasurer may also do so in exigent circumstances, but the sum or measure must be reviewed and ratified by the Commission within 90 days.

In addition to the existing requirement that the DFI certify reports from public depositaries, the DFI must provide information or data as may be required by the Commission.

The Commission is required to maintain a single depositary pool and treat public depositaries uniformly without regard to differences in their charters.

New Public Depository Requirements:

The Commission may establish the required amount of eligible securities that a public depository must pledge and segregate.

Public depositories must provide the exact status of its capitalization, collateral, and liquidity, in addition to the existing requirement of providing information about its net worth.

Public depositories must notify the Commission of an event which causes its net worth to be reduced in an amount greater than 10 percent, from within five working days to within 48 hours, or by the close of business of the following business day.

A public depository's liability is not altered by a merger, takeover, or acquisition, except if liability is assumed by agreement or law by the successor entity or resulting financial institution.

Rulemaking:

In 2009, at the direction of the Commission, the Office of the State Treasurer initiated and adopted permanent rule changes to bring Public Deposit Protection Commission rules into alignment with Substitute House Bill 2061. Through the formal rule-making process, OST repealed Washington Administrative Code (WAC) 389-12-260 and amended WAC 389-12-010 through WAC 389-12-320.

The new rules allow reciprocal certificate of deposit programs to accept public deposits in Washington State, and establish a temporary mechanism with which to assess liability in the unlikely event that another bank failure causes an assessment prior to December 31, 2009.

The amendments to Title 389-12 are available on the OST website (<http://www.tre.wa.gov/PDPC/pdpc.htm>).

Insured Deposits and FDIC Issues

In addition to changes to state laws associated with Public Deposit Protection Commission rules, the State Treasurer strongly advocated the extension of enhanced federal deposit insurance - the Transaction Account Guarantee (TAG) program.

The TAG program has been an important tool to reach this new level of protection. More than half of the public deposits in Washington are insured by the FDIC through the program and therefore do not require collateral at a time when liquidity is critical to our banking system.

The TAG program was slated to expire December 31, 2009, which would have forced banks that may still be struggling to provide much higher levels of collateral to secure public deposits at one hundred percent.

The State Treasurer has been in regular contact with the FDIC urging them to extend the TAG program. OST also worked closely with state regulators, state and corporate treasurers, and the banking community to actively support the extension which allows more time for economic recovery to take hold and greater stability to return.

Adding six months to this important program helped solidify a still fragile economic recovery by helping improve the confidence both public and private sector depositors have in their financial institutions.

This summer the Treasurer outlined his concerns and rationale for requesting an extension to FDIC chairwoman Sheila Bair. See Appendix

On August 27, the Federal Deposit Insurance Corporation's Board of Directors voted unanimously to extend the Transaction Account Guarantee Program until June 30, 2010. By insuring non-interest-bearing deposits larger than the \$250,000, this program has been invaluable in our effort to protect nearly \$8 billion of public deposits.

Looking Ahead:

The Office of the State Treasurer continues to work with state and federal regulators to keep abreast of changing conditions in public depositaries as the nation faces challenges as the economy regains its footing.

The office continues to work with financial institutions, local governments and local government depositors to understand how to maximize FDIC insurance and transition to use of collateral in the additional time provided by the extension of the TAG program.

By the end of 2009, the PDPC is scheduled to complete implementation of electronic reporting for Monthly & Quarterly reports to the PDPC.

In the first half of 2010, OST will implement an exit strategy for the TAG program. This will reduce reliance on FDIC coverage for Non-Interest Bearing Transaction Accounts and increase collateral to cover accounts no longer fully insured (e.g., NOW Accounts).

Timeline:

January 16, 2009 - Bank of Clark County closed (Public Deposit Protection Act initiated for 1st time in 40 year history).

- DFI - State Bank Regulator - closed bank and designated FDIC as Receiver.
- FDIC - Sold Bank of Clark County (BCC) to Umpqua Bank of Roseburg, Ore. (Insured deposits only).
- FDIC - Provided public depositors with "insured" & "secured" (collateral pledged by BCC) funds
- FDIC - Provided public depositors with Receivership Certificates for the "unsecured" portion (the "Loss").
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February 3, 2009 - PDPC calculated each remaining bank's portion of the "unsecured."

- Deposits to be assessed to the pool of depositaries & notified each of their shares.

Note: PDPC was required to wait for December 31 reports (filed January 31) showing each banks public deposit balance (most recent report per statute). Reports from 12/31/08

showed approximately \$8 billion in public deposits with an estimated \$800 million in pledged collateral.

February 6, 2009 - PDPC assessed 90 Banks for “unsecured” public deposits (\$15.144 million).

- Deposits provided account information for wire transfer.

February 6, 2009 - Banks were required to remit share of loss in two business days.

Tuesday, February 10, 5 p.m. - All banks remitted payment.

Wednesday, February 11- Thursday February 12 – PDPC reimbursed public depositors remaining portion of lost deposits in exchange for assignment of Receivership Certificates issued by the FDIC. Public deposits restored within 30 days of failure.

The closure of Bank of Clark County highlighted the necessity for updating Washington’s system for protecting public deposits. With that in mind, the State Treasurer implemented an action plan to modernize the safeguards and requirements of financial institutions that are allowed to accept public deposits.

Considerations:

- Top Priority – Continued safety and security of public tax dollars.
- State & local governments access to their accounts to conduct the public’s business.
- Healthy banks and thrifts form an important underpinning of the state’s economy.
- State & local governments are struggling to make every dollar stretch (budgetary pressure).
- Financial institutions face growing challenges in an increasingly difficult economic environment.
-

February 18, 2009 – PDPC adopted Resolution 2009-1 requiring public depositaries to collateralize their uninsured public deposits at 100 percent by June 30. Goal was to better protect public deposits without threatening the viability of our financial institutions with additional assessments if failure occurs.

Concerns (as result of 100 percent collateral requirement):

- Banks may choose to limit level of public deposits to rebalance liquidity and collateral.
- Banks may decide public deposits are not financially viable.
- Banks may only accept “insured” deposits to limit required collateral levels.

February 20, 2009 – The State Treasurer requested additional information from banks and thrifts including:

- Enhanced monthly reporting – All Banks (Deposits, Securities Pledge, Net Worth, Loans / Assets).

- Established semi-monthly reporting – Most challenged financial institutions.

March 6, 2009 – SHB 2061 signed into law (Statutory Changes to Chapter 39.58 RCW). The new law:

- Merged thrift and bank pools into a single, stronger pool.
- Improved the ability to protect confidential information provided to OST by bank regulators related to the health of financial institutions.
- Redefined maximum liability in terms of uninsured deposits rather than total deposits.
- Provided flexibility to make rule changes to create more safe investment options for local governments, the reciprocal CD program for example.

April 7, 2009 – PDPC adopted Resolution 2009-2 requesting OST to initiate rulemaking needed to amend the Washington Administrative Code (WAC) to:

- Bring program rules into alignment with the new statute.
- Allow implementation of reciprocal deposit programs to provide additional fully insured interest earning opportunities to public depositors.
- Establish a temporary mechanism with which to assess liability through the risk pool in the unlikely event another bank failure causes an assessment before all uninsured deposits are collateralized (i.e., Total public deposits vs. Uninsured public deposits).

April 30, 2009 – OST adopted new rules (WAC 389-12) that took effect immediately as emergency rules allowing Reciprocal Deposit Programs (such as CDARS) to provide governments options to invest larger sums in CDs – but in a way that is fully insured by the FDIC.

May 8, 2009 – Westsound Bank Closed.

- DFI – State Bank Regulator – closed bank and designated FDIC as Receiver.
- FDIC – Sold Westsound to Kitsap Bank (ALL deposit transaction).
- PDPC – No action necessary.

Note: All of Westsound's public deposits were 110 percent collateralized.

June / July 2009

- OST and PDPC worked with Financial Institutions to move toward the 100 percent collateral of uninsured deposits.

July 23, 2009 – Adopted Permanent Rules (WAC 389-12) – Following a 4 month process.

- Filed Pre-proposal (Intent) on April 17 (Published in WSR on May 6).
- Filed Proposed Rules on June 11 (Published in WSR on July 1).
- Solicited comments from public depositaries on June 12.
- Held Public Hearing on July 22 @ 1:00 p.m.

- 3 Banks represented (Union / Cashmere Valley / Heritage).
- Filed Permanent Rules on July 23 (Published in WSR on August 19).
- Effective 31 days after filing (August 23).

Note: Emergency Rules effective through August 28

Benefits of Reciprocal Programs:

- Reduce / Eliminate the need for deposit collateralization
- Capitalize on available FDIC Insurance
- Create yield opportunities for local governments

Other steps taken in administration's first 100 days:

- Held regular meetings with DFI to discuss the eighty state-chartered banks.
- Retained consultants to act as liaisons for banks & local governments.
- Engaged in regular communications with County Treasurers to discuss banking issues in their communities.
- Encouraged regulators to consider systemic risk of bank failures on Washington's pooled system (i.e., "least cost model").
- Encouraged regulators to extend increased insurance coverage beyond 12/31/09.
- Monitored bank ratings issued by rating services

August / September 2009 - Revised reporting requirements for financial institutions.

- Monthly - Focus on Liquidity Measures (i.e., Brokered Deposits, FHLB Advances, etc.)
- Quarterly - Focus on Capital Measures (i.e., Non-Performing Assets, Capital Ratios, etc.)

October 9, 2009 - FDIC distributed dividends to BCC depositors for claims on lost deposits.

- FDIC sold loans in auctions to private investors and other institutions.
- 40+ BCC customers were refunded \$4.79 million of \$20.77 million in uninsured deposits.
- PDPC received approximately \$3.5 million of \$15.1 million (23 percent) in lost deposits.
- Monies were rebated to banks based on previous assessments on October 20.

September 11, 2009 - Venture Bank closed

- DFI - State Bank Regulator - closed bank and designated FDIC as Receiver.
- FDIC - Sold Venture Bank to First-Citizens Bank and Trust Company (ALL deposit transaction).
- PDPC - No action necessary.

Note: all of Venture Bank's public deposits were 110 percent collateralized

November 6, 2009 - United Commercial Bank closed.

- DFI - State Bank Regulator - no action (Bank located in CA)
- FDIC - Sold United Commercial Bank to East West Bank (ALL deposit excluding certain brokered deposits transaction)
- PDPC - No action necessary.

Note: all of United Commercial Bank's public deposits were collateralized

Other developments:

By December 31, 2009:

- Implement electronic reporting for Monthly & Quarterly reports to the PDPC
- Pilot to financial institutions - November 2009

By June 30, 2010 - Exit Strategy for TAG Program

- Reduce reliance on FDIC coverage for Non-Interest Bearing Transaction Accounts (TAG Program).
- Increase collateral to cover accounts no longer fully insured (e.g., NOW Accounts).

Note: We are seeing a number of financial institutions come back into the public funds market place, in large part due to their renewed confidence in the public deposit system. They are once again accepting public funds, and are taking steps to offer more competitive rates. We are working with financial institutions to help them take these steps as quickly as possible.

History and Description of the Washington Public Deposit Protection Act

The 1969 the Legislature enacted Chapter 193 establishing the Public Deposit Protection Act which created the Public Deposit Protection Commission.

The Act was implemented on August 11, 1969, by adopting temporary rules. On February 9, 1970, the Commission adopted permanent rules for administration of the Act in accordance with the Washington Administrative Code (WAC).

Prior to the Act, each bank was required to execute a collateral agreement with each public treasurer having a bank account. To guarantee against loss, the bank, after allowance for Federal Deposit Insurance Corporation (FDIC) insurance, was required to place securities in escrow having a value equal to 110% of each public treasurer's bank account balance.

With the passage of the 1969 legislation, in the event of default of one bank, all participating banks in the state of Washington will collectively assure that no loss of funds will be suffered by any public treasurer or custodian of public funds. The original Act dictated that each bank's collateral of pledged securities was reduced from 110% to 5% of the public treasurers' bank account balances.

In 1977 a review of the provisions of the Act by the Legislature resulted in the increase of the collateral requirement from 5% to 10% and clarified language about collateral replenishment.

In 1983, the Act was expanded to allow savings banks and savings and loan associations to become public depositories. A separate collateral pool was created for these new public depositories.

In 1984, at the request of the Commission, the Legislature amended the Act to allow a public treasurer to maintain deposits in excess of a depository's net worth as long as the depository pledged collateral in an amount equal to 100% of the excess deposits. It also limited total public deposits in one institution to 300% of its net worth. Total public deposits in each financial institution could not exceed 30% of the aggregate public funds on deposit of all treasurers statewide. An institution could exceed these limits only if it pledged 100% collateral for the excess.

In 1986, the Legislature passed two bills amending the Act. One reduced the limitation of total public funds on deposit in a depository to 150% of its net worth or 30% of total public funds on deposit statewide, whichever amount is less, and allowed the Commission to establish regulations setting forth minimum financial standards for public depositories. The other provided that the Commission, or the chair upon delegation by the Commission, may authorize public treasurers to have out-of-state or alien bank accounts for operating purposes or receipt of revenue. Public funds deposited in out-of-state or alien bank accounts are not protected from loss under the Act.

In 2005, at the request of the State Treasurer, the Legislature amended the Act to allow the Commission, or the chair upon delegation by the Commission, to authorize accounts in out-of-state and alien banks for certain higher education endowment funds for a specified instructional program or research project. In the event of the default of a public depository, the Commission establishes the amount of public fund loss.

THE COMMISSION

The Public Deposit Protection Commission consists of the State Treasurer, as chairman, the Governor, and the Lieutenant Governor. The State Treasurer is designated chairman, and the administration of the Act is assigned to the Office of the State Treasurer.

DUTIES

The Commission has the statutory authority to make and enforce regulations necessary for the performance of its functions under the Act. The Commission is empowered to request a public depository to furnish information on its public deposits and the exact status of its net worth. The Commission is further empowered to take any action deemed advisable for the protection of public funds and to establish procedures for collection or settlement of claims arising from loss.

Each depository reports monthly and quarterly to the Commission the aggregate amount of all public deposits and the amount of collateral pledged in accordance with a single agreement. Those depositories having excess deposits or those not meeting the minimum financial standards set by the Commission must monitor public deposits on a daily basis and maintain adequate collateral accordingly.

Under the Act, all public treasurers and other custodians of public funds are relieved of the responsibility of executing tri-party agreements, reviewing pledged securities, and authorizing additions, withdrawals, and exchanges of collateral. Similarly, financial institutions no longer need to review the status of each public fund balance and the collateral pledged under numerous tri-party agreements.

DEFINITIONS

Public Funds: moneys under the control of a treasurer or custodian belonging to, or held for the benefit of, the state or any of its political subdivisions, public corporations, municipal corporations, agencies, courts, boards, Commissions, or committees, including moneys held as trustee, agent, or bailee.

Public Depository: a financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has been approved by the Commission to hold public deposits, and which has segregated for the benefit of the Commission eligible collateral having a value of not less than its maximum liability. The addition of the word "bank" denotes a bank, trust company, or national banking association and the word "thrift" denotes a savings association or savings bank.

Treasurer: the state treasurer, a county treasurer, a city treasurer, a treasurer of any other municipal corporation, and any other custodian of public funds.

Trustee: a third-party safekeeping agent who has completed a depositary pledge agreement with a public depositary and the Commission. Such third-party safekeeping agent may be the federal reserve bank of San Francisco, the federal home loan bank of Seattle, the trust department of the public depositary, or such other third-party safekeeping agent approved by the Commission.

IN CASE of LOSS

Definitions

The statute defines a loss as the issuance of an order by a regulatory or supervisory authority or a court restraining a depositary from making payments of deposit liabilities, or the appointment of a receiver for a public depositary.

The Commission rules define the date of loss as one of the following situations, whichever occurs first:

- Taking possession of the depositary by a supervisory agency;
- Appointment of a receiver or conservator for a depositary;
- Commencement of proceedings for a voluntary liquidation;
- The date an order is issued by a regulatory agency or a court restraining a depositary from making payments on deposit liabilities; and,
- The date the Commission declares that a depositary is unable to repay public deposits in full.

Certification and Verification

When a loss occurs, the receiver is required, within 20 days after taking possession of a public depositary, to certify to the Commission the amounts on deposit by each public depositor. Within 10 days after receiving the certification, each public depositor must supply the Commission with a verified statement of its deposits as disclosed by its records. The Commission is then responsible for fixing the amount of such public deposits and, after deducting any allowable FDIC insurance, assessing the balance of the loss against all public depositaries.

Assessment

The Commission assesses the collateral pool to reimburse public treasurers for deposits not covered by federal deposit insurance. If necessary, the failed depositary is assessed the entire amount of its collateral. If this does not cover the losses, the balance of the depositaries in the pool is assessed proportionately up to their maximum liability on the date of the failure. Since commercial banks and thrift institutions have separate collateral pools, only the depositaries in the same pool as the failed depositary are assessed.

Assessments are payable on the second business day following demand and, in the event of failure to pay, the Commission is empowered to take possession of, and liquidate, securities pledged as collateral.

Amounts subsequently received from distribution of the remaining assets of the depositary shall first be paid to the public depositors to the extent of any unpaid net deposit liability, and then to the public depositaries against which assessments were made in the same proportion as the assessments. Any expense incurred by the Commission in the course of liquidation is paid as a liquidation expense of the depositary in which the loss occurred.

FINAL BILL REPORT

SHB 2061

C 9 L 09

Synopsis as Enacted

Brief Description: Concerning the powers of the public deposit protection commission in regard to banks, savings banks, and savings associations as public depositaries.

Sponsors: House Committee on Financial Institutions & Insurance (originally sponsored by Representative Kirby; by request of State Treasurer).

House Committee on Financial Institutions & Insurance

Background:

Public funds may be deposited only in banks and thrift institutions that have been approved as public depositaries by the Public Deposit Protection Commission (Commission). The Commission is comprised of the Governor, the Lieutenant Governor, and the State Treasurer.

The State Treasurer chairs the Commission and provides administrative support. The Commission is responsible for protecting all public funds deposited in public depositaries. "Public funds" are those moneys belonging to or held for the state, its political subdivisions, municipal corporations, agencies, courts, boards, commissions, or committees, and includes moneys held in trust.

A "public depositary" is a financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes, which has been approved by the Commission to hold public deposits, and which has segregated eligible collateral having a value of not less than its maximum liability. There are separate collateral pools maintained for banks and thrifts.

The Commission's powers include:

- requiring any public depositary to furnish information dealing with public deposits and the exact status of its net worth;
- taking action for the protection, collection, compromise or settlement of any claim arising in case of loss of public funds;
- establishing requirements for qualification of financial institutions as public depositaries, and other terms and conditions under which public deposits may be received and held;
- setting criteria establishing minimum standards for the financial condition of bank and thrift depositaries and, if the minimum standards are not met, providing for additional collateral requirements or restrictions regarding a public depositary's right to receive or hold public deposits;

- fixing the official date on which any loss shall be deemed to have occurred;
- and in case loss occurs in more than one public depository, determining the allocation and time of payment of any sums due to public depositors.

To be approved as a public depository, a financial institution must meet minimum requirements of the Commission and must pledge securities as collateral to protect public funds on deposit in all public depositories (not just for that particular institution). For the first 12 months as a public depository, a depository must pledge and segregate eligible securities of at least 10 percent of all public funds on deposit in the depository. If deposit insurance and collateral pledged by a failed institution are insufficient to reimburse all public depositors, the other public depositories are each assessed a proportionate share of the shortfall.

The Commission may require the State Auditor or the Department of Financial Institutions (DFI) to investigate and report on the condition of any financial institution applying to become a public depository. The Commission may also require an investigation and report on the condition of any public depository. The DFI must also advise the Commission of any action the agency has directed a public depository to take which will result in a reduction of greater than 10 percent of the net worth of the depository. A public depository must notify the Commission within five working days of any event that causes a reduction of greater than 10 percent in the net worth of the depository.

Summary:

Powers of the Commission.

The Commission is given "broad administrative discretion" in performing its general powers. The Commission may delegate all of its authority to the State Treasurer, except rulemaking. The Commission may assess costs or deny, suspend, or revoke authority to hold public funds, if a public depository fails to: provide, or allow verification of, required information; or comply with relevant laws and rules or policies of the Commission.

In addition to the existing requirement that the DFI certify reports from public depositories, the DFI must provide information or data as may be required by the Commission. Any information or data provided to the Commission by a financial institution or a federal or state regulatory agency, must be maintained in the same confidential manner and have the same protections as examination reports received by the Commission from the DFI.

The Commission is required to maintain a single depository pool and treat public depositories uniformly without regard to differences in their charters.

Public Depository Requirements . The Commission may establish the required amount of eligible securities that a public depository must pledge and segregate.

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Public depositories must provide the exact status of its capitalization, collateral, and liquidity, in addition to the existing requirement of providing information about its net worth. Public depositories are required to provide the Commission with the uninsured amount of public funds on deposit in each report. They also must notify the Commission of

an event which causes its net worth to be reduced in an amount greater than 10 percent, from within five working days to within 48 hours, or by the close of business of the following business day. A public depository's liability is not altered by a merger, takeover, or acquisition, except if liability is assumed by agreement or law by the successor entity or resulting financial institution.

Maximum Liability.

The "maximum liability" of a public depository means, with reference to a public depository's liability for loss per occurrence by another public depository, on any given date a sum equal to 10 percent of:

- all uninsured public deposits held by a public depository that has not incurred a loss by the most recent Commission report date; or
- the average of the balances of uninsured public deposits in the last four reports.

An additional way of defining "maximum liability" is also included to mean a sum or measure that the Commission may set by resolution according to criteria established by rule.

The State Treasurer may also do so in exigent circumstances, but the sum or measure must be reviewed and ratified by the Commission within 90 days. If a public depository is 100 percent collateralized by eligible collateral, the "maximum liability" of a public depository that has not incurred a loss may not exceed the 10 percent sum mentioned above. The definition of "maximum liability" does not limit the authority of the Commission to adjust the collateral requirements of public depositories.

Reporting.

The State Treasurer is required to report to the Legislature on actions taken by the Commission and the State Treasurer regarding public deposit protection by December 1 of each year.

Votes on Final Passage:

House 97 0

Senate 49 0

Effective: March 6, 2009

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This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

[View full bill as passed by the Legislature here.](#)

**Washington Public Deposit Protection Commission
OLYMPIA, WASHINGTON**

RESOLUTION NO. 2009-1

WHEREAS, significant stress in the global financial industry and worsening national and international economic conditions are affecting the state's financial institutions and local governments. This commission's purpose is to oversee the Public Deposit Protection Commission (PDPC) member institutions in a way that fulfills its statutory purpose to protect public deposits should a loss occur. This commission must adopt more up to date policies and procedures to best protect public deposits mindful of the challenges that come when large institutions like Washington Mutual, and smaller ones such as Bank of Clark County encounter difficulties; and

WHEREAS, this commission is committed to act in a forward looking manner so that assessments on participating public depositories can be avoided to the greatest extent possible. Thus, in response to the exigent circumstances stemming from national and international economic and financial conditions, and based on the authority granted by law to this commission.

NOW THEREFORE BE IT RESOLVED that all public depositories shall by June 30, 2009, take all measures necessary to fully collateralize its uninsured public deposits at 100%.

As determined by reports provided to the commission, a public depository that cannot make due progress toward collateralizing its uninsured deposits at 100% by June 30, 2009, shall stop accepting new public deposits in uninsured accounts.

In the event a public depository ceases to participate in the PDPC it shall disgorge all public funds in an orderly, lawful and businesslike manner upon notification of disqualification.

The Office of the State Treasurer shall be delegated the authority necessary to carry out this resolution.

BE IT FURTHER RESOLVED that legislation has been introduced at the request of the State Treasurer for consideration by the 2009 Legislature to modernize and improve the laws pertaining to public deposit protection to address the shared concerns of this commission, the Department of Financial Institutions, public depositors, and the banking industry regarding implementation of the PDPC's collateralization and assessment requirements and procedures.

The PDPC urges the Legislature to pass the proposed legislation now under consideration by both the House and Senate, as has been jointly developed by the Office of the State Treasurer and the Department of Financial Institutions with significant input from the financial community.

The PDPC further urges the House and Senate to each incorporate this resolution into the legislative record to be kept in association with this legislation.

IN ACCORDANCE WITH THE PROVISIONS of Chapter 39.58 RCW and Chapter 389-12 WAC, this Commission does hereby grant to the Office of the State Treasurer the authority to carry out the terms of this Resolution and that this Resolution shall become effective February 18, 2009.

ADOPTED at an open meeting of the Washington Public Deposit Protection Commission at Olympia, Washington, after notice thereof duly and regularly given as required by law, this eighteenth day of February, 2009.

**WASHINGTON PUBLIC DEPOSIT PROTECTION COMMISSION
OLYMPIA, WASHINGTON**

RESOLUTION No. 2009-2

WHEREAS, significant progress has been made by financial institutions and public depositors to reach the targets set in the Public Deposit Protection Commission's (Commission) Resolution No. 2009-1 to fully collateralize their uninsured public deposits by June 30, 2009; and

WHEREAS, substantial challenges remain for both financial institutions and public depositors in this difficult time; and

WHEREAS, in keeping with the Commission's request, the Washington State Legislature passed and the Governor signed SHB2061 on March 6, 2009 to improve and modernize the way public deposits are protected.

NOW THEREFORE BE IT RESOLVED, that the Commission request the Office of the State Treasurer initiate, at the earliest time allowed by law, the rulemaking needed to amend the Washington Administrative Code (WAC) to:

Bring program rules into alignment with the new statute,

Allow the implementation of reciprocal deposit programs now permitted by state law so as to provide additional fully insured interest earning opportunities to public depositors, and

Establish a temporary mechanism with which to assess liability through the risk pool in the unlikely event another bank failure causes an assessment before all uninsured deposits are collateralized.

BE IT FURTHER RESOLVED, the Commission appreciates the Legislature's timely passage of SHB2061, the Governor's prompt signature, and the collaboration undertaken by the Office of the State Treasurer and the Washington State Department of Financial Institutions on these matters. The Commission encourages such effective collaboration continue as further work is done to strengthen and improve the protections afforded to public deposits in Washington State;

AND BE IT FURTHER RESOLVED that this Resolution shall become effective April 7, 2009.

ADOPTED at an open meeting of the Washington Public Deposit Protection Commission at Olympia, Washington, after notice thereof duly and regularly given as required by law, this seventh day of April, 2009.

Washington Public Deposit Protection Commission
OLYMPIA, WASHINGTON

RESOLUTION NO. 2009-3

WHEREAS, significant progress has been made by financial institutions and public depositors to safeguard public funds; and

WHEREAS, substantial challenges remain for both financial institutions and public depositors in this difficult time.

NOW, THEREFORE, BE IT RESOLVED that public depositaries are required to make due progress toward collateralizing 100 percent of their uninsured deposits by June 30, 2009. This requirement shall remain in effect until such time as the Commission, by Resolution, sets a different requirement.

BE IT FURTHER RESOLVED that any public depository that does not make due progress toward collateralizing 100 percent of their uninsured deposits by June 30, 2009, shall upon notification by the Office of the State Treasurer stop accepting new public deposits in uninsured accounts until such time as the public depository complies with this requirement.

BE IT FURTHER RESOLVED, for the purpose of this resolution, “due progress toward collateralizing” shall mean (1) attaining 100 percent collateralization of uninsured deposits by June 30, 2009, or (2) complying with the directives of the Office of the State Treasurer in attaining 100 percent collateralization of uninsured deposits within a time frame set by the Office of the State Treasurer that considers the facts and circumstances of a public depository’s inability to achieve 100 percent collateralization by June 30, 2009.

BE IT FURTHER RESOLVED that the Commission appreciates the quick and decisive action taken by financial institutions, public depositors, and state and federal regulators in safeguarding public funds by strengthening and improving protections afforded to public deposits in Washington State.

AND BE IT FURTHER RESOLVED that this Resolution shall become effective June 9, 2009.

ADOPTED at an open meeting of the Washington Public Deposit Protection Commission at Olympia, Washington, after notice thereof duly and regularly given as required by law, this ninth day of June, 2009.

DRAFT RESOLUTION

EXTENSION OF FDIC INSURANCE COVERAGE

Support for FDIC's proposed amendment to extend guarantee of deposits held in qualifying noninterest-bearing transaction accounts until at least June 30, 2010

WHERE the National Association of State Treasurers resolved March 8,
AS, 2009 to urge the Federal Deposit Insurance Corporation (FDIC) and other regulators to recognize the key role of public deposits when the FDIC acts to strengthen and support financial institutions at this challenging time for the nation's economy;

WHERE approximately \$700 billion in public and private funds deposited
AS, nationwide in fully insured accounts covered by the Transaction Account Guarantee (TAG) program now provides an important source of liquidity for many financial institutions; and

WHERE FDIC has proposed rulemaking to extend the Transaction
AS, Account Guarantee program to June 30, 2010, which in many instances will strengthen protections for public funds by maintaining full insurance coverage for qualifying noninterest-bearing accounts until economic conditions improve;

Now therefore be it resolved, that the National Association of State Treasurers supports FDIC's proposed amendment to extend the Transaction Account Guarantee program until June 30, 2010 to provide added stability and predictability at this still-fragile time for the economy and the financial system on which it depends. We further encourage FDIC to consider a longer extension to December 31, 2010 to allow more time for economic conditions to improve;

Be it further resolved, that the National Association of State Treasurers encourages State Treasurers to communicate with financial institution regulators and industry representatives about how this proposed extension will effectively sustain the safety and security of public funds in their states; and

Be it further resolved, that the National Association of State Treasurers urges State Treasurers to provide official comment to FDIC in support of the proposed extension of the Transaction Account Guarantee program by July 30, 2009.

July 17, 2009 Letter to FDIC

July 17, 2009

Sheila Bair, Chair
Federal Deposit Insurance Corporation
550 17th St NW
Washington D.C.

Notice of Proposed Rulemaking regarding Possible Amendment of the Temporary Liquidity Guarantee Program to Extend the Transaction Account Guarantee Program with Modified Fee Structure

Dear Ms. Bair,

I am writing to strongly support the extension of the Transaction Account Guarantee (TAG) program beyond its current December 31, 2009 expiration date, though I would prefer the extension were for a full year. The Washington Bankers' Association, the Community Bankers' Association, the Financial League and our state bank regulator all join me in full support of this extension. While our economy's rate of decline appears to be slowing and some positive signs are emerging, the economy and the financial system are both still fragile. Extending TAG will provide more time for economic growth to take hold and for our struggling financial institutions to regain their footing.

Our key interest is the safety and security of public funds, which can best be achieved by bolstering our financial institutions and spurring economic recovery. We passed new legislation and are applying strong oversight here in Washington state – in partnership with banking regulators, the financial industry, and government depositors – to reduce risks and liabilities for financial institutions and restore confidence among local government depositors. We set the goal for all public depositories to set aside 100 percent collateral for uninsured public deposits by June 30, 2009 and are happy to report that all 103 public depositories with over \$8 billion in public funds on deposit have reached this new higher collateral level.

The TAG program plays a major role in our efforts to strengthen protections for public funds by giving financial institutions a way to accept large public deposits in fully insured accounts that do not require collateral. Of \$8.2 billion in public deposits, nearly 55 percent – \$4.5 billion – is now in fully insured accounts. This gives financial institutions that serve as public depositories an added source of liquidity and also helps provide additional confidence and strength to private-sector depositors too.

Adopting your alternative to extend the TAG program allows more time for financial institutions to regain the capacity to offer government depositors longer-term interest bearing options – especially if public depositors can move to programs like CDARS, only recently made available to our government depositors by changes to state law and rules. And, if you can find a way for FDIC to exclude reciprocal programs like CDARS from the definition of brokered deposits, more institutions can accept public deposits which can help facilitate a smoother transition away from reliance on the TAG program.

Our cash-strapped state and local governments need reliable banking services and investment options. They rely on interest earnings to pay for public services. We all need strong, stable and reliable financial institutions to provide public depositors with competitive rates and services whenever possible. Your proposal to extend the TAG program beyond its scheduled December 31st 2009 expiration date can help sustain the progress we have made, especially if it is possible to make this a 12 month extension.

It would be especially helpful if you can announce your decision as soon as possible. It is a fragile time for financial institutions, their customers, and the economy as a whole. Because many are already planning their future investments, deposit maturities and business activities through the end of the year, early action to extend the TAG program would add stability and strength to the economy. If you choose not to extend TAG, an early announcement will afford us more time to prepare for the end of the program in December.

We have made a lot of progress to better protect public funds while also reducing risks and liabilities for financial institutions, but much remains to be done at this still challenging time. Thank you for your help. Please do not hesitate to contact me directly should you have any questions or concerns.

Sincerely,

James L. McIntire,
Commission Chairman and Washington State Treasurer