

Approved

3/27/91
Date

MINUTES OF THE SENATE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE

The meeting was called to order by RICHARD L. BOND at _____
Chairperson

9:00 a.m./~~p.m.~~ on THURSDAY, MARCH 21, 1991 in room 529-S of the Capit

All members were present ~~except~~:

Committee staff present:

Bill Wolff, Research Department
Fred Carman, Revisors Office
Louise Bobo, Secretary

Conferees appearing before the committee:

Representative J.C. Long
Grant Brooks, Kansas Banking Department

Chairman Bond called the meeting to order at 9:12 a.m.

HB 2250 - Banking: concerning examinations, preparing for exit reviews.

Representative J.C. Long addressed the committee in favor of this bill. He stated that this legislative proposal would require an exit review after bank examinations, require examination reports be sent to the examined bank, and require that minutes be kept of the meeting. Rep. Long stressed that these exit reviews were extremely useful in providing guidelines for the bank and setting sound bank policy. (Attachment 1)

Grant Brooks, Kansas Banking Department, appeared in support of the concept of the bill but had concerns with the language. Mr. Brooks stated that the bill, as currently written, (1) mandated exit meetings with the bank's board of directors and these meetings were often unnecessary and difficult to schedule, (2) the bill does not specify who is responsible for taking the minutes at these meetings, and (3) the bill permits use of a court reporter at these meetings. Mr. Brooks also requested the committee to amend HB 2250 to add language which would allow state banks to own stock in Kansas Bankers Surety Company. He explained that HB 2132, introduced during the 1990 session, would have allowed this but the bill did not survive the deadline and thus was never enacted. (Attachment 2)

During the discussion which followed, a committee member asked Mr. Brooks about using a tape recorder at the exit reviews. Mr. Brooks responded that tape recorders are easily altered and they (the commission) would stop the meeting if one were used. Mr. Brooks said that a verbatim transcript usually anticipates litigation and these exit review meetings are supposed to be an educational tool for the bank. Chairman Bond pointed out that this bill gives the management of a bank some authority to request an explanation as to what is wrong with the bank and why it was not given a higher rating.

Senator McClure made a motion to make the exit review meeting optional on the part of the Commissioner and the Board of Directors. Senator Reilly seconded the motion. The motion carried.

Senator Strick made a motion to allow the bank to be responsible for taking the minutes at all exit review meetings. Senator Reilly seconded the motion. The motion carried.

Senator Salisbury made a motion to strike the language stating that the minutes may be taken by a certified shorthand reporter. Senator Reilly seconded the motion. The motion carried.

Senator Salisbury made a motion to add a new section to HB 2250 to incorporate the language in HB 2132 and to change the title of HB 2250 to reflect investments.

Senator Yost informed the committee that it had been brought to his attention that there was nothing in HB 2059 to prohibit a bank from another state coming into Kansas and he

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE,
room 529-S, Statehouse, at 9:00 a.m.^{XXX} p.m. on THURSDAY, MARCH 21, 19⁹¹.

offered an amendment which would take care of this oversight. A member inquired why that had not been included in HB 2059. Chairman Bond stated that, because of the controversies and complexities surrounding interstate banking, it was the choice to keep HB 2059 free of amendments, get it passed, and then clean it up later if necessary. He further explained that Senator Yost's proposed amendment would prohibit a bank from moving into Kansas without capital investment and would also make them subject to banking regulations and the privilege tax. Mr. Brooks requested that the language "and amendments thereto" be added to the amendment.

Senator Yost made a motion, seconded by Senator Reilly, to amend HB 2250 to prohibit interstate banking and to incorporate Mr. Brook's request. The motion carried.

Senator Yost made a motion to recommend HB 2250, as amended, favorable for passage. Senator Salisbury seconded the motion. The motion carried.

The meeting adjourned at 9:58 a.m.

SENATE COMMITTEE

ON

FINANCIAL INSTITUTIONS AND INSURANCE

OBSERVERS
(Please print)

Thursday, Mar 21, '91

DATE	NAME	ADDRESS	REPRESENTING
3/21/91	FRANK D. DUNNICK	Topeka	STATE BANK Commissioner
"	Gent L. C. Brooks	"	Commissioner's Counsel
"	Sam May	"	KBA
"	J. C. Lopez	"	Rep 105 th
"	Jewel Wright	Topeka	Ks Credit Union League

STATE OF KANSAS

J. C. LONG
HOUSE OF REPRESENTATIVES
ONE HUNDRED FIFTH DISTRICT
Harper, Barber,
Kingman and Sumner Counties



TOPEKA

HOUSE OF
REPRESENTATIVES

COMMITTEE ASSIGNMENTS
MEMBER: COMMERCIAL AND FINANCIAL INSTITUTIONS
FEDERAL AND STATE AFFAIRS
TAXATION
LEGISLATIVE JUDICIAL AND
CONGRESSIONAL APPORTIONMENT

TESTIMONY ON HOUSE BILL 2250

CHAIRMAN BOND MEMBERS OF THE COMMITTEE:

House Bill 2250 is a refreshing change from issues such as interstate banking and the KPERS problem. House Bill 2250 in most respects codifies practices of the bank commissioner.

House Bill 2250:

>requires an exit review after bank examinations;

>requires examination reports be sent to the examined bank;

>provides minutes to be kept at the exit review by methods agreed upon by the banks board of directors or the commissioners office.

In my 10 years as a member of a board of directors and serving seven years on the House Commercial and Financial Institutions Committee, I have discovered that these exit reviews are extremely helpful in guiding and setting sound bank policy. These meetings allow for interaction between the bank board and the examination team. It allows the bank board to understand the banks rating, why a bank is rated in this manner and helps the bank board further develop a working and constructive relationship with the regulatory agency.

Thank you, Chairman Bond and members of the committee for the opportunity to appear before you today in support of House Bill 2250.

STATE CAPITOL
TOPEKA, KANSAS 66612-1591
(913) 296-7672
TOLL FREE: 1-800-432-3924

Attachment 1
F I V I
P.O. BOX 472
HARPER, KANSAS 67058-0472
(316) 896-2890

3/21/91

HOUSE BILL No. 2250

By Representative Long

2-13

9 AN ACT relating to banks and ~~banking, concerning examinations,~~
10 ~~providing for exit reviews,~~ amending K.S.A. 1990 Supp. 9-1701 ✓
11 and repealing the existing section.
12

the banking code;

13 *Be it enacted by the Legislature of the State of Kansas:*

14 Section 1. K.S.A. 1990 Supp. 9-1701 is hereby amended to read
15 as follows: 9-1701. (a) The commissioner or the commissioner's as-
16 sistant or examiners shall visit each bank and trust company at least
17 once every 18 months, and may visit any bank or trust company if
18 the commissioner deems it necessary, for the purpose of making a
19 full and careful examination and inquiry into the condition of the
20 affairs of such bank or trust company. For such purpose the com-
21 missioner, the commissioner's assistant and examiners are authorized
22 to administer oaths and to examine under oath the directors, officers,
23 employees and agents of any bank or trust company. Such exami-
24 nation shall be reduced to writing by the person making it and such
25 person's reports shall contain a full, true and careful statement of
26 the condition of such bank or trust company. The commissioner in
27 lieu of making a direct examination and inquiry may accept the
28 examination and report of an authorized federal agency. *The com-*
29 *missioner shall provide to the board of directors of the bank or trust*
30 *company a copy of the examination report written by the state*
31 *examiners or the report of the federal agency.* Neither the com-
32 missioner, the commissioner's assistant nor any examiner shall ex-
33 amine any bank or trust company in which the person making such
34 examination is a stockholder or is otherwise financially interested or
35 to which bank or trust company or any officer thereof the person
36 making the examination is indebted.

37 (b) ~~The commissioner~~ examination team shall conduct an exit
38 review meeting with the board of directors of a bank or trust com-
39 pany following the examination provided in subsection (a), of such
40 bank or trust company. ~~Accurate minutes~~ Minutes shall be kept
41 at all exit review meetings. Minutes of the exit review meeting may
42 be kept by a certified shorthand reporter, if the board of directors
43 of such bank or trust company or the bank commissioner determines

- 3. 1 *it necessary.*
- 2 ~~Sec 2.~~ K.S.A. 1990 Supp. 9-1701 is hereby repealed.
- 4. 3 ~~Sec 3.~~ This act shall take effect and be in force from and after
- 4 its publication in the statute book.

Sec. 2. (a) No bank the home office of which is located outside the state of Kansas shall establish or operate a branch bank within the state of Kansas.

(b) For the purpose of this section "branch bank" means any office, agency or other place of business, at which deposits are received, checks paid or money lent.

(c) For the purpose of this section "bank" means an insured bank as defined in section 3(h) of the federal deposit insurance act, 12 U.S.C. 1813(h). *and so forth.*

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Testimony

Before

The Senate Committee on Financial
Institutions and Insurance

by Conferee:

Grant L.C. Brooks, General Counsel

Kansas Banking Department

Chairman Bond and Committee members, House Bill 2250 embodies a very sound concept. However, the State Banking Department does have some concerns with the language. The bank members of this Committee know that the bank examiner always hold a meeting with the bank management and management always is made aware of the tentative results of an examination report. The Commissioner only meets with the board of directors of a bank if that bank is considered a problem bank. The language of this bill mandates exit meetings with the bank's board of directors. I am sure that this Committee can see the problem that this creates with rural banks. It may be very difficult to gather a bank's board of directors and sit them down for a meeting. If this bank is not a problem bank, the meeting would neither be an efficient use of the department's time nor an efficient use of the bank's board of directors' time. Additionally, the bill does not specify who is responsible for the taking of minutes at these meetings. I presume the intent was that the bank's board of directors' secretary take minutes of these meetings. However, the Commissioner would be more comfortable if this statute specifically states who is responsible for taking the minutes.

Attachment 2
F I & I
3/21/91

Consequently, the State Banking Department respectfully requests the Committee consider amending this bill to make an exit review meeting with the bank's board of directors optional upon the request of either the bank or the Bank Commissioner and that the responsibility to take minutes is specifically given to the bank's board of directors.

Once again, Mr. Chairman and Committee members, the State Banking Department appreciates the sincere and valid concerns embodied in this piece of legislation. We are just requesting some fine tuning in order for it to work perfectly.

The last concern the Commissioner has is with the language that permits use of a stenographer to record the meeting. The mere fact that somebody wants a verbatim transcript of a meeting usually indicates anticipated litigation or at least they want to use what was said. The exit meeting is used as an educational tool for a bank. It is used to inform bank management of the tentative findings of an examination and to suggest ways of improving bank management skills. The use of a court reporter, in my opinion, turns an otherwise informative meeting into an adversarial meeting, and this defeats the purpose for even having the meeting.

Consequently, the State Bank Commissioner would respectfully request that this language be deleted from this bill. If this language remains in this bill, I shall advise the Commissioner that the department's Counsel must be at every meeting where the bank requires a stenographer be present because the use of a stenographer turns an otherwise informational meeting into an adversarial meeting.

Once again, Chairman Bond and Committee members, we agree with the underlying concept of communication between regulators and banks. The solutions that I have suggested for this piece of legislation are needed to lay the foundation for a more harmonious relationship between regulators and bankers, and I am confident that this Committee will give these considerations the attention they deserve.

The Banking Department has one further request and asks for your indulgence in this matter. House Bill 2132 would amend the General Power's section of the banking code to allow state banks to own stock in the Kansas Bankers Surety Company. Unfortunately, this bill was tabled in the House Committee. This department would respectfully request that this Committee consider amending the bill, before you today, to include language that would allow state banks to own stock in Kansas Bankers Surety Company. In order to completely understand this request, some background is necessary.

During last year, as a result of a FDIC examination, it was discovered that many Kansas banks own stock in Kansas Bankers Surety Company. However, K.S.A. 9-1101 does not authorize state banks to hold such an equity investment. Kansas Bankers Surety provides all types of financial institution liability insurance policies to state banks. This company was incorporated in 1909 by a number of state banks. Also at that time, state banks would not own such stock. Therefore, the state banks formed trusts to hold the stock. The trustee was usually the bank's cashier. Over time the trustees died or moved on and the stock was apparently put in the name of the bank and was not listed as an asset of the respective bank. So, today 67 stockholders of Kansas Bankers Surety are state banks and hold 55,692 shares worth \$1,670,760. The state bank shareholders hold this investment as a nonbook asset.

It would serve no purpose to force state banks to divest themselves of this nonbook stock and would, in fact, harm Kansas Bankers Surety.

The State Bank Commissioner would like to have this regulatory issue resolved by an amendment to the bill before you that would allow state banks to buy this stock.

Finally, one point of concern is the banking code does have a statute that imposes criminal liability and forfeiture of office for a Commissioner that permits an ongoing violation of the banking code. So, without an amendment to the bill, before you, allowing state banks to own stock in the Kansas Bankers Surety Company, the Commissioner arguably has to require the banks divest themselves of this stock, otherwise, he may subject himself to penalties.

THANK YOU FOR YOUR TIME AND CONSIDERATION.

HOUSE BILL No. 2132

By Committee on Commercial and Financial Institutions

2-5

8 AN ACT relating to banks and banking; concerning the general
9 powers thereof; investments; amending K.S.A. 1990 Supp. 9-1101
10 and repealing the existing section.

11

12 *Be it enacted by the Legislature of the State of Kansas:*

13 Section 1. K.S.A. 1990 Supp. 9-1101 is hereby amended to read
14 as follows: 9-1101. Any bank hereby is authorized to exercise by its
15 board of directors or duly authorized officers or agents, subject to
16 law, all such powers, including incidental powers, as shall be nec-
17 essary to carry on the business of banking, and:

18 (1) To receive deposits and to pay interest thereon at rates which
19 need not be uniform. The state bank commissioner, with approval
20 of the state banking board, may by regulations of general application
21 fix maximum rates of interest to be paid on deposit accounts other
22 than accounts for public moneys;

23 (2) to buy and sell exchange, gold, silver, foreign coin, bullion,
24 commercial paper, bills of exchange, notes and bonds;

25 (3) to buy and sell bonds, securities, or other evidences of in-
26 debtedness of the United States of America or those fully guaranteed,
27 directly or indirectly, by it, and general obligation bonds of the state
28 of Kansas or any municipality or quasi-municipality thereof, and of
29 other states, and of municipalities or quasi-municipalities in other
30 states of the United States of America. No bank shall invest an
31 amount in excess of 15% of its capital stock paid in and unimpaired
32 and the unimpaired surplus fund of such bank in bonds, securities
33 or other evidences of indebtedness of any municipality or quasi-
34 municipality of any other state or states of the United States of
35 America: (a) If and when the direct and overlapping indebtedness
36 of such municipality or quasi-municipality is in excess of 10% of its
37 assessed valuation, excluding therefrom all valuations on intangibles
38 and homestead exemption valuation; (b) or if any bond, security, or
39 evidence of indebtedness of any such municipality or quasi-munic-
40 ipality has been in default in the payment of principal or interest
41 within 10 years prior to the time that any bank acquires any such
42 bonds, security or evidence of indebtedness;

43 (4) to make all types of loans, including loans on real estate,

2-5

1 as are adopted by the state bank commissioner pursuant to K.S.A.
2 9-1713, and amendments thereto, to promote safe and sound banking
3 practices, a bank may establish a subsidiary which engages in the
4 following securities activities: (a) selling or distributing stocks, bonds,
5 debentures, notes, mutual funds and other securities, (b) issuing and
6 underwriting municipal bonds, (c) organizing, sponsoring and op-
7 erating mutual funds, (d) acting as a securities broker-dealer; and

8 (23) to subscribe to, acquire, hold and dispose of stock of any
9 class of the federal agricultural mortgage corporation, a corporation
10 having as its purpose the acquisition, holding and disposition of loans
11 secured by agricultural real estate mortgages. No bank's investment
12 in such corporation shall exceed 5% of its capital stock, surplus and
13 undivided profits and such investment shall be carried on the books
14 of the bank as directed by the commissioner; and

15 (24) to subscribe to, buy and own stock in an insurance company
16 incorporated prior to 1910, under the laws of Kansas, with corporate
17 headquarters in this state, which only provides insurance to financial
18 institutions. The investment in such stock shall not exceed 2% of the
19 bank's capital stock, surplus and undivided profits.

20 Sec. 2. K.S.A. 1990 Supp. 9-1101 is hereby repealed.

21 Sec. 3. This act shall take effect and be in force from and after
22 its publication in the statute book.

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THE KANSAS BANKERS SURETY COMPANY

By Bonnie Pinick

This year the Kansas Bankers Surety Company has been in business for eighty-one years.

Because this is the only bonding company owned by the banks and bankers it serves, it might be interesting to trace some of the history of the company. The Company today plays a unique role of serving the banks in eleven mid-western states because of the foresight of a few leading bankers in the state of Kansas.

In 1909, the Kansas Legislature enacted a law establishing the "bank depositor guaranty fund of the state of Kansas." The purpose was to guarantee depositors against the insolvency of the insured institution. The fund was authorized by law, but was created by the funds of the participating members.

Membership into the guaranty fund was purely voluntary. Even though state law permitted national banks to participate, federal law prohibited national banks from membership. In addition, many state banks chose not to become members of the fund. The result was a division of banks in Kansas into three groups: state insured banks, state uninsured banks and national uninsured banks. Naturally, the banks in the latter two groups had more than an idle curiosity as to what the impact of the insured banks would be. Would depositors only put their money into insured banks? Not wanting to wait to see what would happen, leaders in the banking community began taking steps to meet the situation should it become necessary.

On April 29, 1909 the Bankers Deposit, Guaranty and Surety Company was formed and on January 10, 1910 began writing business. The purpose of the company was twofold: to issue surety bonds guaranteeing the deposits of the participating banks; and to execute fidelity bonds on behalf of individual bank officers and employees.

The company continued writing surety and fidelity bonds until 1922. At that time, the insured banks deemed it no longer necessary or profitable to continue writing deposit insurance. The company was reorganized with all of the capital stock of the company placed in over 700 Kansas banks on a pro-rata basis. The company name was changed to the Kansas Bankers Surety Company.

The company continued to grow over the years and to serve the needs of Kansas banks. In 1979 the company had all of the business available or that they wanted to write in Kansas. So the company considered writing other coverages besides Bond & D&O or expanding geographically.

The company decided to expand geographically in 1980 into Missouri, 1981 into Nebraska and Wisconsin, 1985 into Oklahoma, Colorado and Wyoming, 1986 into Iowa and South Dakota and in 1988 into Minnesota and Illinois. In 1910, the premiums written were \$28,446. In 1989, the premiums written were over \$20,000,000.

Of the approximate 12,000 banks in the United States, the company writes Financial Institution Bonds and Directors and Officers Policies for 2,448 banks. That represents roughly 1 out of every 5 banks in the United States, although all of the insured banks are community banks in the Midwest.

Kansas Bankers Surety Company also provides security training programs and seminars for bank employees and risk/exposure surveys for individual banks.

The company has operated profitably over the past 80 years and has returned profits to shareholders by means of dividends. In 1979 when the company expanded into other states there were 32,000 shares of stock outstanding which were held by 454 shareholders with capital and surplus of \$1,572,869. By the spring of 1990 the capital and surplus was \$13,507,260. Most of the current 502 stockholders of the company are banks or active bankers. A few shares of the stock, which have passed through the families of early Kansas bankers, are now spread throughout the country. There are stockholders living as far away as Hawaii.

From the beginning in 1909 to the current date, the Board of Directors of the Kansas Bankers Surety Company have been active bankers.

The purpose of Kansas Bankers Surety Company is to provide insurance protection to banks for losses which may be incurred under the terms of various policies issued by the company. In its 80 years of operation, the company is known for its prompt payment of direct claims to banks. The first embezzlement claim was in the amount of \$738.65. Claims incurred in 1989 were in excess of \$6,000,000. In the last 20 years, one reason for the dramatic increase in claims has been in employee fidelity and, in particular, senior management embezzlement. This is true nationwide.