

MINUTES OF THE Senate Committee on Financial Institutions and Insurance.

The meeting was called to order by Chairperson Dick Bond at 9:04 a.m. on February 2, 1995 in Room 529-S of the Capitol.

All members were present.

Committee staff present: Dr. William Wolff, Legislative Research Department
Fred Carman, Revisor of Statutes
June Kossover, Committee Secretary
Bruce Kinzie, Revisor of Statutes
Richard Ryan, Legislative Research Department

Conferees appearing before the committee: Senator Jerry Moran
William Grant, State Banking Department
Sally Thompson, State Treasurer

Others attending: See attached list

Senator Steffes moved to approve the minutes of the meeting of February 1 as submitted; Senator Corbin seconded the motion. The motion carried.

Chairman Bond opened the hearing on SB 9, relating to certain requirements of the municipal investment pool (MIP) fund. Senator Jerry Moran, sponsor of this legislation, explained that the bill was introduced as a result of an inquiry from a banking constituent in his district. Senator Moran requested answers to three questions from State Treasurer Sally Thompson concerning the MIP and, based on the reply from the Treasurer's office, he then requested legislation to be drafted to change reporting requirements from "periodic" to "monthly." (Attachment #1) The State Treasurer is now providing information on a monthly basis but, according to Senator Moran, the law should be amended to comply with current practice. Senator Bond inquired of Senator Moran if the language actually requires a mark to market notice to all participants and Senator Moran referred to the language on page 2, line 2 of the bill. Senator Moran stated that he supports the MIP and feels it serves local units of government well.

Senator Steffes observed that the concerns with the MIP began when interest rates began to climb and agreed that full public disclosure is a necessity.

In response to Senator Hensley's question, Senator Moran stated that it was his desire to keep politics out of this matter.

The hearing on SB 9 was suspended to allow William Grant, State Banking Department, to request introduction of legislation in response to passage of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. (Attachment #2) Senator Steffes made a motion to introduce this legislation. Senator Lawrence seconded the motion; the motion carried.

The hearing on SB 9 was resumed with State Treasurer Sally Thompson providing the committee with an update on the status of the MIP. (Attachment #3)

Chairman Bond responded to the earlier reference to political motivation by stating that it is not the intent to "politicize" an issue of this importance, and that he believes the MIP should continue. He also stated that it is to be expected that a number of amendments will be offered during the course of the hearings and this committee will consider those suggestions.

Ms. Thompson stated that the MIP has faced a crisis since interest rates began rising, but the pool has survived and is stable. She also outlined steps she has taken to insure the survival of the MIP:

1. Maturities have been shortened. Only 7% of the pooled money was invested in four year maturity; however, the 10 month norm was not short enough.
2. A very short term "overnight pool" has been created to take advantage of current interest rates.
3. Longer term (2 year) securities have been exchanged with idle funds for less than 1 year securities.
4. Securities have been sold before maturity and reinvested at current interest rates. The trading loss on selling early is expected to be offset with earnings from the higher rate.
5. State idle funds have been included in the MIP to stabilize the fund. While the idle funds may experience a delay in earnings, it should be very small and short-lived.

CONTINUATION SHEET

MINUTES OF THE Senate Committee on Financial Institutions & Insurance, Room 529-S Statehouse, on February 2, 1995.

Ms. Thompson advised that she has discussed the proposed amendments with staff and her reaction is that the legislature should not move too quickly. The office of the State Treasurer conducted a survey of pool participants and, of the 107 responses, 75% stated that they are satisfied with the functioning of the MIP and 80% did not support changes in the legislation this year; all believed the pool should be continued. Most of the anticipated amendments, according to Ms. Thompson, are already part of policy. Ms. Thompson voiced concern about the cost of engaging a financial investment counselor and again urged the committee not to move forward too quickly until it can be determined that the changes will be right for the future.

Senator Steffes asked whether out-flow currently exceeds in-flow and Ms. Thompson responded that the fund will be down again by a net amount of \$30 million due largely to one participant taking \$22 million out in January to test the stability of the MIP. Senator Steffes observed that the pool was not currently paying the federal rate of 5.79 and Ms. Thompson agreed that a few participants could withdraw their money and earn a higher rate by direct investing but that there is a built-in penalty for withdrawing 90 day investments early, for instance. The Treasurer also agreed that core deposits are not as much as they have been in the past.

In response to Senator Hensley's question, Ms. Thompson replied that other states are all studying and looking at the problem and agreed there should be restrictions on taking out money.

Senator Praeger observed that money management should occur within the framework of what can be controlled and the question arises of whether to minimize income to minimize risk. Senator Praeger also noted that the pooled money ought to be able to get a favorable rate without putting the money at risk. The Treasurer responded that in no month has the rate been lower than the previous month.

Ms. Thompson responded to Senator Clark that there has been one instance where a penalty was assessed a school district for early withdrawal; however, the penalty was not significant, and that the MIP board makes policy that details how the treasurer makes investments.

Senator Steffes noted that participants are happy with the MIP but the problem is that when the market changed, the state picked up the tab and asked, if there were no state funds available, what would the estimated loss have been to municipalities. Ms. Thompson stated that today there would be very little loss, perhaps \$5 to 7 million, which prompted Senator Steffes to ask why there was a \$100 million transfer from general funds. The response was that it was needed to bring the pool rate up closer to the market rate and to put additional funds back into the pool. Senator Steffes stated that, in other words, the state is keeping the MIP solvent and, in his opinion, the pool should not have an unfair advantage over local banks, which should have first access to the deposits.

Senator Bond stated that the committee would be interested in the language developed by national conferences, etc., to regulate municipal investment pools; however, the MIP is a Kansas creation and no personal affront should be taken if changes are now necessary to our "recipe." Changes will not only affect the current treasurer, but future treasurers, and are not intended as an affront to the current State Treasurer.

Due to the shortage of time, the hearing will be continued to to the next meeting, scheduled for Monday, February 6. The committee adjourned at 9:56 a.m.

SENATE FINANCIAL INSTITUTIONS & INSURANCE
COMMITTEE GUEST LIST

DATE: 2/2/95

NAME	REPRESENTING
Craig Husting	Johnson County Treas. Office
Wm E. O'BRIEN	" " TREASURER
LARRY TUCKER	RENO COUNTY TREASURER
Sally Thompson	State Treasurer
Tom Wilder	Insurance Dept
MIKE BILLINGER	HAYS KS
Perry McCabe	McPherson USD #18
Alan STEPPAT	PETE McCOILL + Assoc.
Mike Montero	Alan Cobb
David Ross	Ks. Assn. LIFE UNDERWRITERS.
Roger Franzele	FIC
Darin Duffin	State Treasurer's Office
Peggy Hanna	State Treasurer's Office
ROGER CLARK	CITY OF WICHITA
Norm Wilks	RASB
Jonathan Simon	State Treasury
Jim M... ..	KBA
Chuck Stokes	KBA
William GRANT, Judi STORK	OFF. STATE BANK COMM.

Frank Dummer, Kevin Genderning ✓

FOR YOUR INFORMATION
JERRY MORAN

May 24, 1994

Honorable Jerry Moran
State Senator, 37th District
Emprise Bank Building
P.O. Box 128
Hays, Kansas 67601

Dean Senator:

Treasurer Thompson has forwarded to me your letter of May 13, 1994, to respond to your questions regarding the Municipal Investment Pools. We welcome requests such as yours, as it gives us the opportunity to share some of our experiences and successes, as well as to assist in the education of those who care enough to take an interest in the endeavors they took part in creating.

To answer your questions, it will be necessary to relay quite a bit of information to you. This is why we requested to visit with you personally, to be sure your queries are fully satisfied, as well as to deliver this letter for future reference. I will attempt to address your questions in the order in which you presented them.

1. If I understand the "current participant weighted average maturity" and the "current investment weighted average maturity" correctly, it seems there is a significant difference between those weighted averages in terms of days. Is there a problem if the participating municipalities withdraw their funds at their maturity?

We do not feel that there is a problem if participating municipalities withdraw their funds at maturity. Much more goes into the prudent management of a portfolio than simply matching known sources and uses of funds. In fact, a simple matched book strategy carries risks as

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Attachment #1

great or greater than a managed portfolio, but typically with lower yielding results. When the Pool was originated, we were aware that a matched book strategy would be one most of our participants could understand, as well as probably replicate on their own. We felt, however, that this strategy did not provide the municipalities the opportunity to share the expertise, skills, and experience of the State Treasurer's investment staff, while it also mitigated the advantages of pooling funds to achieve economies of scale. Thus, our plan, both then and now, is to conduct careful cash flow analysis and forecasts, and actively manage the portfolio based on such analysis. This is the same type of analysis a commercial bank or savings institution would estimate to determine their "core deposits", which would be eligible to extend into somewhat longer maturities than those determined to be "hot money", and kept virtually liquid in extremely short maturities.

There are several factors that have historically affected the weighted average terms for both the participant's funds and the portfolio's investments. These are factors which we have observed during the twenty months of the pool's operation, and we have yet to see much variance in these factors, even though we have experienced both falling and rising interest rates. Let's start with the participant's funds.

Although we always try to maintain sufficient liquidity to meet all participant's maturities, it is an extremely rare day that all participant's maturities are actually withdrawn from the pool. Much more commonly, the majority of participant's maturities are rolled over into new dates, generally for a week to a month. While this keeps the measure of the weighted average maturities of participant's funds extremely short, in practice, the funds are actually left in the pool for much longer periods of time than the maturities dates would indicate.

Another factor which allows us to extend investment maturities longer than deposit maturities is the fact that the pool has become large enough and utilized actively enough that practically every day in which the pool operates sees new deposits into the pool. Due to municipalities' funding flows, we have been able to determine that, on an average basis, we are able to utilize some of the incoming funds to fund maturing deposits from other municipalities.

Additionally, in the event that we have estimated incorrectly, we do have the statutory authority and market ability to execute reverse repurchase agreements to raise short term liquidity to meet daily funding needs. This is a commonly used short term funding tool which allows us to sell securities from the portfolio, but at the same time, simultaneously contract to repurchase those same securities at some later date at a specified rate. These are typically executed on an overnight basis, i.e., we sell today and repurchase tomorrow. The advantage of using this tool as opposed to an outright permanent sale of securities, is that it allows us to retain the yields on the securities in the portfolio without incurring the risk of reinvesting those proceeds at a lower yield. Also, it allows us to boost the liquidity in the portfolio for the exact amount of time needed, while still paying the lowest rate possible for that liquidity. By this, I mean that in a normal yield curve environment, rates for short term investments are much lower than for those on longer maturities. By utilizing a reverse repurchase agreement, we are able to raise liquidity at a short term rate, while still earning interest on the security at its longer term rate.

A normally sloped yield curve demonstrates this concept clearly. Let us assume that we have purchased a security with a two year maturity which is yielding 5.80% on the current yield curve. Now let us also assume that we find today that we have estimated the pool's outflows too low, and need liquidity to fund the day's withdrawals. By using a reverse repurchase agreement, we could sell our two year security today, receive the cash needed to fund the pool's withdrawals, then repurchase that exact same security tomorrow. Yet the rate we would have paid for the use of those funds overnight would have been more in the area of 4.20%. Thus, even though we were paying 4.20% for liquidity overnight, we were still earning 5.80% on the security sold under a repurchase agreement. In addition, we would not be taking the risk that if we had sold the security outright, then repurchased it in the open market at a later date, it might cost considerably more, and thus provide a lower yield to the pool's participants.

Another factor that inflates the variance between the weighted average maturity of participant's deposits and the pool's investments is the fact that, although we have a number of callable securities in the portfolio, for purposes of calculating weighted average maturity, we use the ultimate maturity date of all securities. Thus, there are a number of securities in the portfolio which will potentially be called anywhere from one to three years prior to their actual maturity date, virtually shortening their actual time to maturity substantially.

A second inflating factor in the average maturity variance is the fact that when calculating the average maturity of investments, only the actual par amount of the security is used in the calculation. In practice, these securities generate interest payments every six months which actually shorten the present value of the cash flows generated from the security. The term used to describe and calculate this present value is called "duration". Although duration is a much better measure of the actual weighted average maturity of a portfolio, we have not been reporting duration in our monthly reports simply because most people not actively involved in institutional portfolio management find the concept somewhat confusing. Nonetheless, since the issue has arisen, we will plan to include it from this point forward. At the current time, the duration of the Short Pool is 1.17 years and the duration of the Intermediate Pool is 1.33 years.

2. What is the current market value of the short term Municipal Investment Pool and the Intermediate Term Municipal Investment Pool? With rising market interest rates, are the values of the investments in the funds decreasing? Would you please provide me information showing the current market value of each individual investment?

The current market value of both pools varies on a day to day and minute to minute basis. The market value is calculated on the prices at which the entire portfolio could be liquidated at one time. In the case of the Short Pool, this would involve pricing some 200 securities every minute or so for every day on which the institutional fixed income markets trade. The closest we can come to actually tracking such prices is to take the New York closing market prices for

each security each day and calculate the market value of the portfolio based on the assumption that the entire portfolio could be liquidated instantaneously at those prices. While this is the most logical assumption to follow, it would also be impossible to accomplish, and thus not realistic. By the time we are able to capture the closing New York prices and calculate market values for the portfolio, those same securities are already trading in Tokyo at prices which may vary significantly from the New York close. In addition, prior to the New York market opening the next morning (which would be our next opportunity to sell securities), these same securities have also been trading in the London market for several hours, experiencing the same type of price fluctuation as they would have in New York and Tokyo earlier.

The other assumption which must be followed to market price a portfolio is that the entire portfolio could be liquidated instantaneously. While the assumption is necessary, it is also ridiculous. If, in fact, we were to liquidate the entire portfolio, it would take several days to solicit competitive bids for those 200 securities and actually get the trades executed. And during that time, the prices on the remaining securities would be constantly fluctuating. The only time we could imagine such an event being necessary is if ALL pool participants decided to make early withdrawals at the exact same time. This would be akin to a run on a commercial bank, right along with all the risks accompanying any forced liquidation.

When our pool participants sign their Pool Participation Agreement, they agree that they will leave their deposits in the Pool until the date they have designated for maturity. This maturity date is supposed to coincide with the amount of time the deposits were offered to the participant's local financial institutions. It is incumbent on the Pool's portfolio managers to rely upon the word of those Pool participants in investing those funds, just as the local financial institutions would have relied on their word when putting a maturity on a CD. Thus, if the Pool participants choose to withdraw their funds prior to the maturity date they have provided, they take the same risks as if they were to cash in a bank CD early (an early withdrawal penalty) or sell a Treasury security prior to maturity and prevailing interest rates had risen since its purchase. Basically, this is the same risk ALL investors take when purchasing ANY fixed income security. This is the same risk a bank would face in a run on deposits, i.e., the necessity of liquidating securities prior to maturity at a loss.

As to rising market interest rates, the portfolios of the Pools are made up of fixed income securities, so as with any fixed income security, when interest rates rise, the price of the security falls. Therefore, the Pool portfolios will exhibit the same type of price fluctuation as a financial institution's fixed income portfolio, i.e., when interest rates rise, prices fall, and vice versa. Thus, over the past few months, the prices on the securities in the Pools have fallen as rates have risen. Nonetheless, the advantage we have over many fixed income portfolios is the percentage of funds in short maturities.

With fixed income securities, the shorter the term to maturity, the less the price is affected by movements in interest rates. The reason for this is that with a shorter duration, you are locked into the rate on the existing security for only a short time before the security matures and the funds become available for reinvestment at the new current rates. Since the Pools are invested primarily in fairly short duration securities, the recent interest rate fluctuations have not

affected the market prices of those securities near so much as if they had been invested in longer duration securities.

It appears that the Federal Reserve Bank has taken a breather from the recent interest rate hikes. They have indicated that they are now at or near a neutral policy on credit accommodation. The consensus among market participants is that the Fed will now leave short rates at current targets until substantial economic data has been received to determine the exact impact of the recent rate hikes.

As for providing current market values for each individual investment, I hesitate to do so based on the flawed assumptions with which they are generated, as well as the fact that such a report would not be current within hours of being generated. The deposits in the Pools change on a daily basis, the investments in the Pools change on a daily basis, and the balances in the Pools change on a daily basis. Thus any report I could provide would be outdated by the time you received it.

As of May 19, 1994 (the last date for which I have market values), the liquidation value of the Short Pool exceeded the pool's principal deposits, and the liquidation value of the Intermediate Pool exceeded the pool's principal deposits less withdrawal penalties.

3. Should the participating municipalities show their investment in the Municipal Investment Pool at market value? It seems that prudent accounting standards would require municipalities to do so.

As per GASB Statement No. 3 (Deposits with Financial Institutions, Investments, and Reverse Repurchase Agreements) in Section 68, Note 11, it is noted as followed:

"If the governmental entity has invested in a pool managed by another government, such as city monies in a state treasurer's investment pool, no disclosure of the individual deposits and investments of the pool is required by this Statement unless the entity owns specific, identifiable investment securities of the pool. Instead, the investment in the pool should be treated as a type of investment with a market value equal to the net realizable value of the entity's share of the pool based on the pool's valuation method."

In Section 6 of that same Statement, it is stated that:

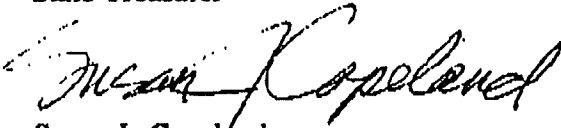
"The entity's share . . . may be based on the market value of the pool's investments or on some other basis used by the pool, such as amortized cost for fixed-income securities."

Both the Short and Intermediate Pools use the amortized cost method for calculating the daily market value of deposits.

Thanks for the opportunity to address your concerns. We hope we have allayed any apprehension you may have felt. If you or your constituents have further questions, please feel free to contact our office.

Sincerely,

SALLY THOMPSON
State Treasurer



Susan J. Copeland
Chief Investment Officer

**PROPOSED AMENDMENTS TO THE KANSAS BANK HOLDING COMPANY ACT AND KANSAS
BANKING CODE IN RESPONSE TO PASSAGE OF THE RIEGLE-NEAL INTERSTATE
BANKING AND BRANCHING EFFICIENCY ACT OF 1994.**

Following this introduction is a series of the proposed amendments to the Kansas Bank Holding Company Act (KBHCA) and the Kansas Banking Code (Code). Each separate section reflects draft amendments which were developed in an attempt to bring Kansas statutes into conformance with the interstate banking provisions of Riegle-Neal which become effective in September of 1995.

The suggested changes are reflected in each section as follows:

- (a) current language proposed for retention is in **normal type**;
- (b) current language proposed to be removed from the statute is ~~stricken~~; and
- (c) new language proposed to be added is ***italicized and underlined.***

This system was used with the intention of allowing a clear and convenient comparison of the old and new language.

Section 1 through Section 14 - proposed amendments to KBHCA which were facilitated by Riegle-Neal's provisions relating to powers of bank holding companies.

Section 15 through Section 17 - proposed amendments to the Code to implement the required statutory authority for Kansas state banks to engage in affiliate agency activities to the same extent that Riegle-Neal allows for national banks.

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Attachment #2

Section 1. Amend K.S.A. 9-519 to read as follows:

For the purposes of K.S.A. 9-520 through 9-524, and amendments thereto, and K.S.A. 9-532 through 9-539, unless otherwise required by the context:

(a)(1) "Bank holding company" means any company:

(A) Which directly or indirectly owns, controls, or has power to vote 25% or more of any class of the voting shares of a company which is or becomes a bank holding company by virtue of this act;

(B) which controls in any manner the election of a majority of the directors of a bank or of a company which is or becomes a bank holding company by virtue of this act;

(C) for the benefit of whose shareholders or members 25% or more of any class of the voting shares of a bank or 25% or more of any class of the voting shares of a company which is or becomes a bank holding company by virtue of this act, is held by trustees; or

(D) which, by virtue of acquisition of ownership or control of, or the power to vote the voting shares of, a bank or another company, becomes a bank holding company under this act.

(2) Notwithstanding paragraph (1), no company:

(A) Shall be deemed to be a bank holding company by virtue of its ownership or control of shares acquired by it in connection with its underwriting of securities if such shares are held only for such period of time as will permit the sale thereof on a reasonable basis;

(B) formed for the sole purpose of participating in a proxy solicitation shall be deemed to be a bank holding company by virtue of its control of voting rights of shares acquired in the course of such solicitation;

(C) shall be deemed to be a bank holding company by virtue of its ownership or control of shares acquired in securing or collecting a debt previously contracted in good faith, provided such shares are disposed of within a period of two years from the date on which such shares could have been disposed of by such company;

(D) owning or controlling voting shares of a bank shall be deemed to be a bank holding company by virtue of its ownership or control of shares held in a fiduciary capacity except where such shares are held for the benefit of such company or its shareholders.

(b) "Company" means any corporation, trust, limited partnership, association or similar organization including a bank but shall not include any corporation the majority of the shares of which are owned by the United States or by any state, or include any individual or partnership.

(c) "Bank" means an insured bank as defined in section 3(h) of the federal deposit insurance act, 12 U.S.C. 1813(h), except the term shall not include a national bank which engages only in credit card operations, does not accept demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others, does not accept any savings or time deposits of less than \$100,000, accepts deposits only from corporations which own 51% or more of the voting shares of the bank holding company or its parent corporation of which the bank engaging only in credit card

operations is a subsidiary, maintains only one office that accepts deposits, and does not engage in the business of making commercial loans.

(d) "Subsidiary" with respect to a specified bank holding company means:

- (1) Any company more than 5% of the voting shares of which, excluding shares owned by the United States or by any company wholly owned by the United States, is directly or indirectly owned or controlled by such bank holding company or is held by it with power to vote;
- (2) any company the election of a majority of the directors of which is controlled in any manner by such bank holding company; or
- (3) any company more than 5% of the voting shares of which is held by trustees for the benefit of such bank holding company or its shareholders.

(e) "Commissioner" means the Kansas State Bank Commissioner.

(f) "Kansas bank" means any bank, as defined by subsection(c) of this section, which, in the case of a state chartered bank, is a bank chartered under the authority of the state of Kansas, and in the case of a national banking association, a bank with its main office located in Kansas .

(g) "Kansas bank holding company" means a bank holding company, as defined by subsection (a) of this section, with total subsidiary bank deposits in Kansas which exceed the bank holding company's subsidiary bank deposits in any other state.

(h) "Out of state bank holding company" means any holding company which is not a Kansas bank holding company as defined in subsection (g) of this section.

(i) "Foreign bank" means any company organized under the laws of a foreign country, a territory of the United States, Puerto Rico, Guam, American Samoa, or the Virgin Islands, which engages in the business of banking, or any subsidiary or affiliate, organized under such laws, of any such company.

Section 2. Amend K.S.A. 9-522 to read as follows:

No bank holding company or any subsidiary thereof shall directly or indirectly acquire or maintain ownership or control of, or power to vote, more than 5% of any class of the voting shares of any bank domiciled in this state or the power to control in any manner the election of the majority of the directors of any bank domiciled in this state which does not both accept demand deposits and engage in the business of making commercial loans.

Section 3. Amend K.S.A. 9-523 to read as follows:

Except for banks whose voting shares are acquired by a bank holding company

pursuant to subsection (b) of K.S.A. 9-520, and amendments thereto, a majority of the board of directors of each Kansas bank domiciled in this state which is a subsidiary of a bank holding company shall be residents of this state.

Section 4. K.S.A. 9-524 to be repealed:

~~No bank which is a subsidiary of a bank holding company and which is domiciled in another state shall be relocated from such other state into this state.~~

Section 5. Amend K.S.A. 9-532 to read as follows:

~~(a) On and after July 1, 1992, a bank holding company located in a state contiguous to this state or in the state of Arkansas or Iowa, with approval of the state banking board, With prior approval of the commissioner, any bank holding company may acquire, directly or indirectly, ownership or control of, or power to vote, any of the voting shares of, an interest in, or all or substantially all of the assets of a Kansas bank having its principal place of business located in this state or of a Kansas bank holding company. located in this state~~

~~(b) For purposes of K.S.A. 9-519 through 9-524, and amendments thereto, and K.S.A. 9-532 through 539, and amendments thereto, a bank holding company is located in that state or jurisdiction in which the total deposits of its banking subsidiaries are largest.~~

~~(c) A bank holding company located in a state or jurisdiction other than this state, proposing to acquire, directly or indirectly, ownership or control of, or power to vote, any of the voting shares of, an interest in, or all or substantially all of the assets of a bank having its principal place of business located in this state, or of a bank holding company located in this state, shall file an application with the state banking board in a form and Request for approval shall be made by filing an application in such form as required by the commissioner, containing the information prescribed by K.S.A. 9-533, and amendments thereto, and by rules and regulations adopted by the state bank commissioner. At the time of filing the application, the applicant shall pay to the commissioner a fee in an amount established by rules and regulations adopted by the commissioner.~~

~~(d) Nothing in this section shall be construed to permit a bank holding company located in a state other than those referred to in subsection (a), to acquire directly or indirectly, ownership or control of, or power to vote, any of the voting shares of, an interest in, or all or substantially all of the assets of a bank or bank holding company located in this state. In the event a bank holding company ceases to be "located" as defined in subsection (b), in a state referred to in subsection (a), the bank holding company shall immediately notify the commissioner of the change in its status and shall, as soon as practical and within not more than two years after the change in its status, divest itself of direct or indirect ownership or control of, or power to vote, any of the voting shares of, an interest in, or all or substantially all of the assets of all Kansas banks and Kansas bank holding companies. A~~

~~bank holding company that fails to immediately notify the commissioner shall be guilty of a misdemeanor and shall be fined \$500 each day beginning the day its status changed and ending the day notification is received by the commissioner.~~

Section 6. Amend K.S.A. 9-533 to read as follows:

An application filed pursuant to ~~subsection (e)~~ of K.S.A. 9-532 shall provide the following information and include the following documents:

(a) A copy of any application by the applicant seeking approval by a federal agency of the acquisition of the voting shares or assets of a Kansas bank ~~having its principal place of business in this state~~ or of any Kansas bank holding company ~~located in this state~~, and of any supplemental material or amendments filed with the application.

(b) Copies of the public sections of the most recent CRA performance evaluations for all banks which are subsidiaries of the applicant which were assigned a rating of "needs to improve record of meeting community credit needs" or "substantial non-compliance in meeting community needs" ~~evaluating performance of such banks under the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq.~~

(c) Statements of the financial condition and future prospects, including current and projected capital positions and levels of indebtedness, of the applicant, ~~its existing subsidiaries,~~ and the Kansas bank or Kansas bank holding company which is the subject of the application filed pursuant to ~~subsection (e)~~ of K.S.A. 9-532.

(d) Information as to how the applicant proposes to adequately meet the convenience and needs of the community served by the Kansas bank or Kansas bank holding company which is the subject of the application filed pursuant to ~~subsection (e)~~ of K.S.A. 9-532 and the communities served by other Kansas banks ~~having their principal places of business in Kansas~~ which are subsidiaries of applicant, in accordance with the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq.

(e) A list of the name and location of each subsidiary bank of the applicant, together with each subsidiary's most recent examination date, and assigned composite CAMEL rating, and information reflecting each subsidiary's total assets, capital ratios, return on assets ratio, and loan to deposit ratios.

(f) Any additional information the commissioner deems necessary.

Section 7. Amend K.S.A. 9-534 to read as follows:

In determining whether to approve an application filed pursuant to ~~subsection (e)~~ of K.S.A. 9-532, the ~~state banking board~~ commissioner shall consider the following factors:

(a) Whether the banks already subsidiaries of the applicant are operated in a safe, sound and prudent manner.

(b) Whether banks already subsidiaries of the applicant have provided adequate and appropriate services to their communities, including services contemplated by the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq.

(c) Whether the applicant proposes to provide adequate and appropriate services, including services contemplated by the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq., in the communities served by the Kansas bank ~~having its principal place of business located in this state~~ or by the Kansas bank subsidiaries of the Kansas bank holding company. ~~located in this state~~

(d) Whether the proposed acquisition will result in a Kansas bank or Kansas bank holding company ~~located in this state~~ that has adequate capital and good earnings prospects.

(e) Whether the financial condition of the applicant or any of its subsidiary banks would jeopardize the financial stability of the Kansas bank or Kansas bank holding company which is the subject of the application.

Section 8. Amend K.S.A. 9-535 to read as follows:

~~(a) The state banking board~~ commissioner shall approve the application if it ~~determines is determined~~ that:

~~(a) The acquisition is authorized by this act;~~

~~(b) the laws of the state or jurisdiction in which the applicant bank holding company is located in effect as of the time the application is filed permit a bank holding company located in this state to acquire, directly or indirectly, the voting shares of, an interest in, or all or substantially all of the assets of a bank having its principal place of business located in such other state or jurisdiction on terms that are substantially no more restrictive than those established under this act; and~~

~~(c) after consideration of the factors~~ the application favorably meets each and every factor prescribed in K.S.A. 9-534, and the proposed acquisition is in the interest of the depositors and creditors of the Kansas bank or Kansas bank holding company which is the subject of the proposed acquisition and in the public interest generally. Otherwise, the application shall be denied.

(b) Within 15 days after the commissioner's approval or denial, the applicant shall have the right to appeal in writing to the state banking board the commissioner's determination by filing a notice of appeal with the commissioner. The state banking board shall fix a date

for hearing, which hearing shall be held within 45 days after such notice of appeal is filed. The board shall conduct the hearing in accordance with the provisions of the Kansas administrative procedure act and render its decision affirming or rescinding the determination of the commissioner. Any action of the board pursuant to this section is subject to review in accordance with the act for judicial review and civil enforcement of agency actions. An applicant who files an appeal to the state banking board of the commissioner's determination shall pay to the commissioner a fee in an amount established by rules and regulations of the commissioner, adopted pursuant to K.S.A. 9-1713 and amendments thereto, to defray the board's expenses associated with conducting the appeal.

Section 9. Amend K.S.A. 9-536 to read as follows:

An applicant filing an application pursuant to ~~subsection (e)~~ of K.S.A. 9-532 also shall be subject to K.S.A. 9-1719 through 9-1724, and amendments thereto, to the extent applicable.

Section 10. Amend K.S.A. 9-537 to read as follows:

The commissioner at any time may review the activities of ~~a any bank holding company with a subsidiary bank in Kansas located in a state or jurisdiction other than this state~~ and its subsidiary banks ~~located in this state~~ to determine if the proposals of the company as stated in the information provided pursuant to ~~subsection (d)~~ of K.S.A. 9-533 are being fulfilled. The commissioner may require the company and such banks to furnish such additional information as the commissioner finds necessary to make such determination.

Section 11. Amend K.S.A. 9-538 to read as follows:

(a) ~~Each bank having its principal place of business in this state which is a subsidiary of a bank holding company located in a state or jurisdiction other than this state shall file with the state bank commissioner a copy of the public section of the bank's most recent CRA performance evaluation under the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq.~~ Each bank holding company with a subsidiary bank in Kansas shall file with the commissioner a copy of the public section of any CRA performance evaluation of the Kansas bank, issued under the federal community reinvestment act of 1977, 12 U.S.C. 2901 et seq., which assigns the Kansas bank a CRA rating of "needs to improve record of meeting community credit needs" or "substantial non-compliance in meeting community credit needs" or which is requested by the commissioner. The copy shall be filed within 30 days of its receipt by the bank from the bank's primary federal financial supervisory agency.

(b) Should any such evaluation assign the bank a rating of "substantial noncompliance in meeting community credit needs", the ~~state bank~~ commissioner shall give appropriate

public notice of that fact. The commissioner also shall notify the pooled money investment board of the bank's rating of substantial noncompliance and thereafter the bank shall not be designated as a depository for any state moneys until such time as the commissioner notifies the board that the bank is no longer assigned such rating.

Section 12. Amend K.S.A. 9-539 to read as follows:

The ~~state bank~~ commissioner shall adopt such rules and regulations as shall be necessary to carry out the intent and purposes of K.S.A. 9-519 through 9-524, and amendments thereto, and K.S.A. 9-532 through 9-539, which shall be known as the bank holding company act. All rules and regulations of general application shall first be submitted by the commissioner to the state banking board for its approval and upon approval shall be filed as provided by article 4 of chapter 77 of the Kansas Statutes Annotated.

Section 13. A new section to read as follows:

No foreign bank shall transact any business, or maintain any branch, agency, office or other place of business in this state.

Section 14. A new section to read as follows:

(a) No out of state bank holding company or any subsidiary thereof shall directly or indirectly acquire ownership or control of, or power to vote, more than 5% of any class of the voting shares of any Kansas bank unless such Kansas bank has been in existence and actively engaged in business for five or more years.

(b) This section shall not prohibit an out of state bank holding company or any subsidiary thereof from acquiring ownership or control of, or power to vote, more than 5% of the voting shares of any Kansas bank which has been organized solely for the purpose of, and does not open for business prior to, facilitating a merger of such Kansas bank with or into a Kansas bank which has been in existence and actively engaged in business for five or more years, or a consolidation of such Kansas bank and one or more Kansas banks which have been in existence and actively engaged in business for five or more years.

(c) This section shall not prohibit an out of state bank holding company or any subsidiary thereof from acquiring ownership or control of, or power to vote, more than 5% of any class of the voting shares any Kansas bank if the commissioner, in the case of a bank organized under the laws of this state, or the comptroller of the currency, in the case of a national banking association, determines that an emergency exists and that the acquisition is appropriate in order to protect the public interest against the failure or probable failure of the Kansas bank.

Section 15. Amend K.S.A. 9-1101 to read as follows:

Any bank hereby is authorized to exercise by its board of directors or duly authorized officers or agents, subject to law, all such powers, including incidental powers, as shall be necessary to carry on the business of banking, and:

new subsection: subject to such rules and regulations as the state bank commissioner may adopt pursuant to K.S.A. 9-1713, and amendments thereto, to promote safe and sound banking practices, to act as an agent and receive deposits, renew time deposits, close loans, service loans, and receive payments on loans and other obligations for any company which is a subsidiary, as defined in K.S.A. 9-519(d) and amendments thereto, of the bank holding company which owns the bank. Nothing in this subsection shall authorize a bank to conduct activities as an agent which the bank or the subsidiary would be prohibited from conducting as a principle under any applicable Federal or State law.

Section 16. Amend K.S.A. 9-1111 to read as follows:

The general business of every bank shall be transacted at the place of business specified in its certificate of authority and at one or more branch banks established and operated as provided in this section. It shall be unlawful for any bank to establish and operate any branch bank or relocate an existing branch except as hereinafter provided.

(a) For the purposes of this section, the term "branch bank" means any office, agency or other place of business located within this state, other than the place of business specified in the bank's certificate of authority, at which deposits are received, checks paid, money lent or trust authority exercised, if approval has been granted by the state bank commissioner, under K.S.A. 9-1602, and amendments thereto. Notwithstanding the provisions of this subsection, any location at which a depository institution, as defined by K.S.A. 9-701, receives deposits, renews time deposits, closes loans, services loans or receives payments on loans or other obligations, as agent, for a bank pursuant to K.S.A. 9-1101(27) or other applicable state or federal law, shall not be deemed to be a branch bank.

Section 17. Amend K.S.A. 9-701 to read as follows:

Definitions. Unless otherwise clearly indicated by the context, the following words when used in this act, for the purposes of this act, shall have the meanings respectively ascribed to them in this section:

new subsection: "depository institution" means any state bank, national banking association, state savings and loan, or federal savings association, without regard to the state where the institution is chartered or the state in which the institution's main office is located.

SALLY THOMPSON
STATE TREASURER



OFFICE OF THE STATE TREASURER
900 SW JACKSON, SUITE 201
TOPEKA, KANSAS 66612-1235
(913) 296-3171 FACSIMILE: (913) 296-7950

February 2, 1995

Thank you. I know that I have discussed the status of the Municipal Investment Pool with nearly everyone in this room. I have invited 165 Legislators to my office for breakfast meetings to talk about the MIP and answer any questions about its management.

The MIP, over the past several months, has faced a crisis. Interest rates in the United States have risen faster and sharper than in any period since 1927. National experts estimate that losses could reach \$1.5 trillion worldwide.

In Kansas we have faced the crisis and we have survived. In order to keep the MIP a viable investment alternative I have implemented a five point plan to restructure our portfolio.

1. **Shortening of Maturities:** (COLORED CHART) If you look at this chart it is evident that our average maturity, before the interest rate surge hit us hard, was 10 months. Some people will say 10 months was too long, but based on our history the 10 month average was the best decision. Sure today with the benefit of 20/20 hindsight we all know it was too long based on the unprecedented surge in interest rates. We used our short term securities to fund withdrawals from the MIP. (CHART) If you look at this chart, you'll see where we are today. An overwhelming majority of our securities mature in 0-3 months. Please note that is the same place we were at one year ago.

2. **Creation of the Overnight Municipal Investment Pool (OMIP):** The OMIP is an investment option developed to allow participants to take advantage of the current interest rate environment and wait out the escalating interest rate. This strategy was developed with the assistance of Overland Park Mayor and Pool participant Ed Eilert.

3. **Exchanges with Idle Fund:** I exchanged longer term maturities in the MIP with shorter term maturities in the state idle fund. The exchange provided much needed liquidity in the MIP and provided the idle fund a fair rate of return. This strategy was developed with the assistance of Bill Caton, a member of the Pooled Money Investment Board.

4. **Restructuring & Re-investing:** I have sold securities before maturity and reinvested those dollars at the current interest rates. I believe the trading loss on selling early will be offset with the earnings from the higher rate.

5. **The State Idle Fund as a MIP participant:** The final step in restructuring was to create stability in the battered fund. By including State idle funds as a participant, the MIP gets a boost in market rate and in a short time the idle fund will benefit from this arrangement. I fully acknowledge that the idle fund may experience a delay in interest earnings, but in a short time that delay will disappear. It may be of some comfort to know that the Legislature will never feel the delay because the State is running about \$1.6 million ahead of consensus revenue estimating projections on interest earnings.

Senate 7/41
2/2/95
Attachment #3

2-Thompson

I am fully aware that many of the decisions I made are not "politically" popular. I do believe, however, that they are the best financial decisions for the future of the Pool and for Kansas taxpayers. These restructuring steps have worked to rebuild the health of the fund. Today the MIP is on solid ground.

I know that there are several people waiting to offer amendments this morning and I respect and appreciate the discussion they bring to the table. I understand there is genuine concern about the future health of this program. I respectfully urge each of you to consider whether now is the right time to open this statute. The MIP has just survived a crisis and it needs TIME to adjust to the restructuring steps. It may be of comfort to know that most of the amendments that I have seen reflect provisions that are already in policy.

I have not determined what permanent structural changes need to be made in order to remain flexible enough to thrive in all interest rate cycles. I do know that the advice I am getting from investment experts in Kansas and around the country is to assess this situation calmly, learn from the mistakes in Orange County, as well as from the experiences of Texas and with our own Pool, and then, without overreacting or oversimplifying, act sensibly.

I have been asked to serve on a task force of the National Association of State Treasurer's to develop new guidelines for local government pools. I will also attend an NCSL-GFOA conference on creating model legislation to govern pools. I am still in a fact finding mode and need more time to determine what is the right direction for the MIP.

In addition, I have a survey, conducted over the past two days by my clerical staff, of MIP members. (HANDOUT) I am providing the raw data as well as the questions asked. You'll note that 107 of the 165 MIP members responded. 75% or (80) participants said they were very satisfied with the MIP. Only (1) participant said they were not satisfied. In addition, 80% or (91) said they did not support legislative changes this year. Of the (12) that believed legislative changes should be made, six of the respondents believed the changes should give the Treasurer more authority and flexibility. All of those responding believe the MIP should continue, primarily because it improves their opportunities to get the best rate on public funds, whether in the Pool or in their local financial institution.

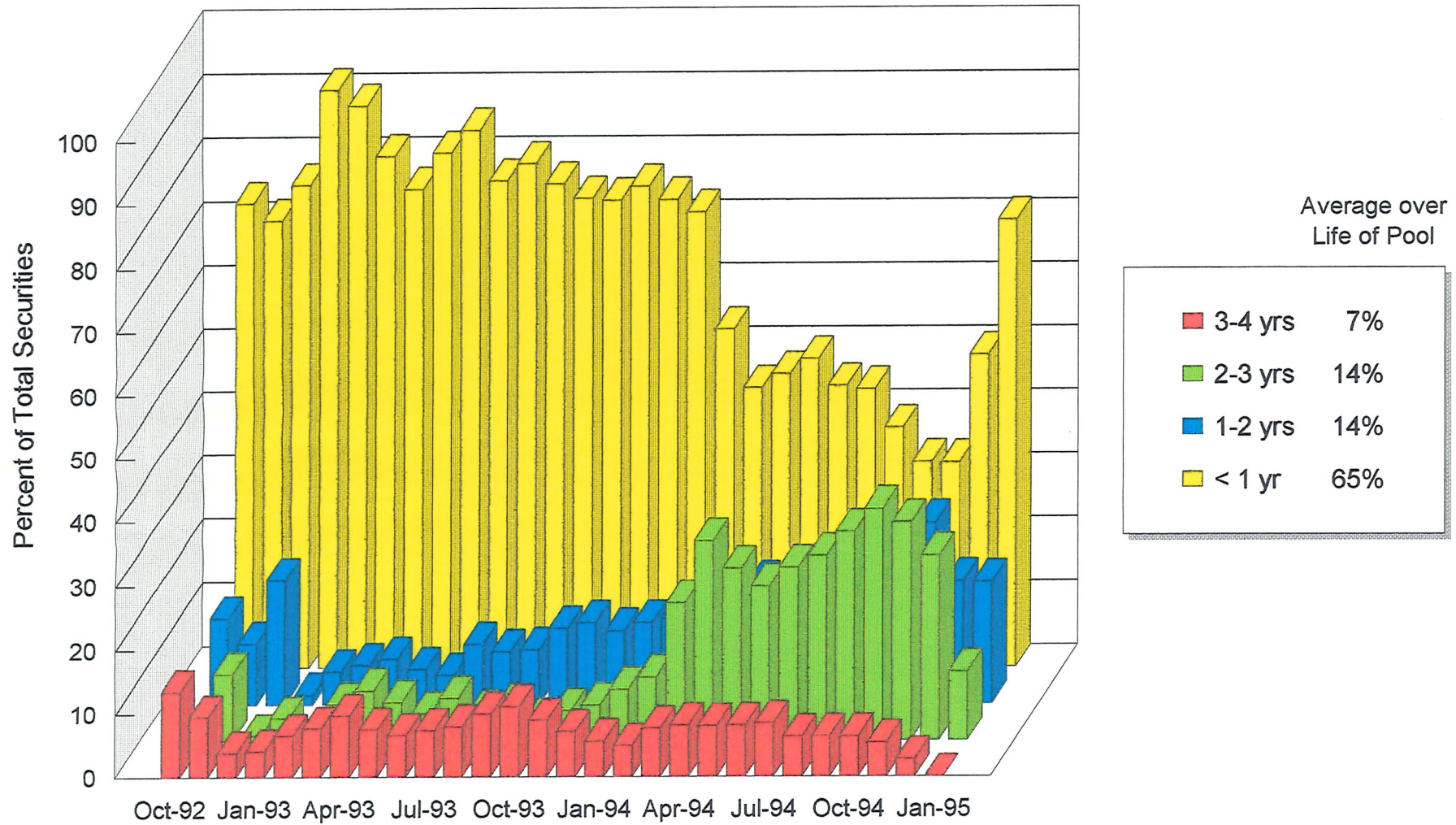
It may be of comfort to know that most of the amendments that I have seen reflect provisions that are already in policy. (1) Market Value (SB 9): Is published in our monthly Pool participant report. (2) The MIP participant advisory committee meets this morning at 10:00am for its first meeting.

As to the qualifications of PMIB members I believe they should be more strident and require all board members, including the Treasurer, to meet certain qualifications. I currently receive investment advice and counsel from a number of different sources, including a performance audit conducted by Mercer Asset Planning, Inc. of Dallas and a recently released Legislative Post Audit. I am concerned about the cost to the participants of contracting services from an investment advisor.

In essence I have already implemented many of these amendments. I know that Senator Bond and Senator Steffes have worked hard to craft these recommendations. I am, however, opposed to moving ahead too quickly to make these amendments a permanent structure until we all have more time to study the impact of these changes over time and through a full interest rate cycle.

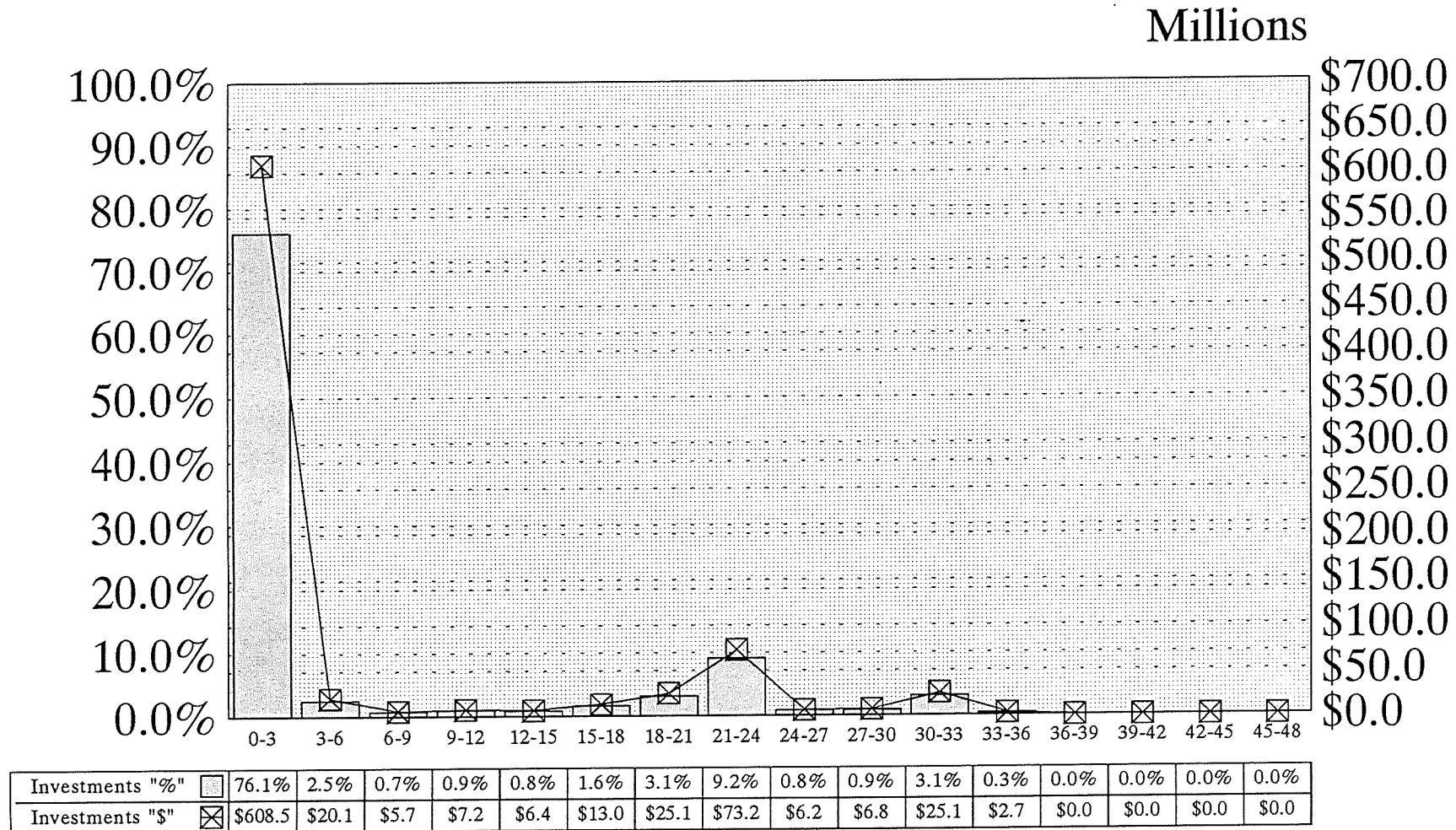
Municipal Investment Pool

Investment Portfolio Structure



Municipal Investment Pool

Risk Diversification by Maturity (by 3-Month Periods)



For the Month Ending January 31, 1995

0-3 Months Includes O/N Investments