Approved: 3/19/96
Date

MINUTES OF THE Senate Committee on Financial Institutions and Insurance.

The meeting was called to order by Chairperson Dick Bond at 9:10 a.m. on March 14, 1996 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

Conferees appearing before the committee: Representative Doug Mays
Rogers Brazier, Office of State Treasurer
Danielle Noe, Kansas Credit Union Association
Matthew Goddard, Heartland Community Bank Association

Others attending: See attached list

Senator Clark made a motion, seconded by Senator Emert, to approve the minutes of the meeting of March 13 as submitted. The motion carried.

The hearing was opened on **HB 2782**, concerning the investment of proceeds of bonds and temporary notes. Representative Doug Mays appeared as a sponsor of this legislation, stating that it amends the statute dealing with the investments of proceeds of municipal bonds and temporary notes to prohibit investments in derivatives. Representative Mays stated that derivatives are risky and volatile and should not be permitted as investment vehicles by Kansas municipalities. (Attachment #1)

Written testimony was submitted by Shirley A. Moses, Director of the Division of Accounts and Reports, State Department of Administration. (Attachment #2)

There were no other conferees; the hearing on **HB 2782** was closed.

The chairman opened the hearing on **HB 2683**, which would restore a provision to the state statute concerning unclaimed funds that was omitted when the statute was rewritten by the legislature in 1994. Rogers Brazier, State Treasurer's Office, explained the changes the bill would make. (Attachment #3) In response to Senator Bond's question, Mr. Brazier advised that credit unions could still impose a fee on less than the $50 amount. The bill will only limit the notification requirement.

Senator Bond suggested that perhaps a time limit should be set beyond which unclaimed funds would escheat to the state. Mr. Brazier advised that, to his knowledge, no other state has such a law and that interest on unclaimed funds remains with the state.

Danielle Noe, Kansas Credit Union Association, testified in support of this bill and provided a brief history of the Disposition of Unclaimed Property Act. She, on behalf of the KCUA, had requested the amendment to raise the value of dormant accounts to $50. (Attachment #4)

Matthew Goddard, Heartland Community Bankers Association, also appeared as a proponent of this legislation, stating that with the passage of **HB 2683**, a demand or savings account would not be presumed abandoned as long as mail to the account owner has not been returned to the sender. (Attachment #5)

The hearing on **HB 2683** was closed. Senator Emert made a motion to raise to $100 the threshold for reporting requirements. Senator Praeger seconded the motion. The motion carried.

Senator Lee moved to pass **HB 2683** favorably. Senator Petty seconded the motion; the motion carried.

The committee returned to consideration of **HB 2782**. Senator Corbin stated his opinion that this legislation is unnecessary. Senator Steffes stated that since the bill relates only to the investment of the proceeds of bonds and temporary notes in narrow amounts of money, he is in agreement with the intent of the bill.

Senator Steffes made a motion to pass **HB 2782** and to place it on the Consent Calendar. Senator Hensley seconded the motion. The motion carried.

The committee adjourned at 9:46 a.m. The next meeting is scheduled for Tuesday, March 19, 1996.

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.

SENATE FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE GUEST LIST

DATE: 3/14/96

NAME	REPRESENTING
Rep Doug Mays	54th Dist, Topeka.
Danielle Noe	KCUA
Matthew Goddard	HCBA
Kathy Taylor	KBA
Linda DeCoursey	KS Insurance Dept
Susan Copeland	STO
Rogers Brazier	St Treasurer
Kelly Kultala	KTLA

STATE OF KANSAS

DOUG MAYS
REPRESENTATIVE, FIFTY-FOURTH DISTRICT
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STATE CAPITOL—ROOM 182-W
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TOPEKA

HOUSE OF
REPRESENTATIVES

COMMITTEE ASSIGNMENTS
CHAIRMAN — RULES AND JOURNAL
VICE CHAIRMAN — LOCAL GOVERNMENT
MEMBER — TAXATION
JUDICIARY
CHAIRMAN — SHAWNEE COUNTY DELEGATION

House Bill 2782

—

Testimony of Representative Doug Mays

House Bill 2782 deals with the investment of bond issues by Kansas municipalities. When a bond issue has been successfully completed, many times there is an intervening period of time before the proceeds are actually appropriated. Kansas law allows the investment of these idle funds and dictates the manner in which they can be invested.

Generally, the statutorily permitted investment vehicles are low risk, fixed income, and short term in nature. Recently, however, I was alarmed to discover that some of the investment institutions approved under one section of the existing statute, were offering, in addition to traditional securities, high risk, interest sensitive derivative products.

Derivatives, as they are commonly known, are not securities in the conventional sense. They invest in nothing. They have no tangible value as is the case with stocks, bonds or mutual funds. Instead, they draw their worth solely from the price or rate of an underling security, commodity, or index. They usually involve leverage, in many cases a great deal. The result is a product of which the value may fluctuate wildly with the up or down movement of the underlining vehicle.

Derivatives are speculative, risky, volatile, and definitely not considered a conservative investment-- as was the original intent of existing law.

The committee may recall the recent bankruptcy of Orange County, California (see attached newspaper articles). This financial disaster, which will ultimately cost California taxpayers, retirees, and vendors hundreds of millions of dollars, was the direct result of derivative speculation with municipal funds.

When this statute was originally passed, the derivatives now allowed did not exist and, I am certain, were not envisioned by the Kansas Legislature. While I am not aware of any instance where losses have occurred as yet, it is only a matter of time.

I ask the assistance of this committee to close up this unforeseen and dangerous loophole before a disaster occurs.

Senate F/+I
3/14/96
attachment #1

BILL GRAVES
Governor

SHEILA FRAHM
Lt. Governor/Secretary

SHIRLEY A. MOSES
Director of Accounts and Reports
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DEPARTMENT OF ADMINISTRATION
Division of Accounts and Reports

MEMORANDUM

DATE: January 23, 1996

TO: Representative Doug Mays

FROM: Shirley A. Moses, Director

SUBJECT: K.S.A. 10-131 Concerning FHLB Securities

I am happy to respond to your research request regarding the issue of unintended loopholes that may exist in K.S.A. 10-131 (f); and, conversely, if the elimination of this section (statute) would severely impede the investment options of a municipality.

The concern is that this statute allows municipalities to invest the proceeds of their bond and note issues in Federal Home Loan Bank (FHLB) obligations. There are at least two issues here: 1) FHLB securities are ***NOT*** backed by the full faith and credit of the U.S. government, (attachment 1); and 2) approximately 25% of the total debt issued by the FHLB is in the "Structured Notes" category. This second risk is the subject of the January 20, 1995 WSJ article "Risky Derivatives are Huge Source of Funds for Federal Agencies" (attachment 2). The key point is here is: ***STRUCTURED NOTES ARE DERIVATIVES*** (attachment 3).

Thus, K.S.A. 10-131 allows municipalities to invest temporary bond and note proceeds in securities that are extremely sensitive to interest rate variations. This sensitivity has the potential to seriously erode principal. Another factor is noted on page 19 of attachment 3: "Because GSE-issued structured debt securities are often tailored to the needs of a particular investor or class of investors, they are generally intended to be held until maturity." This feature alone strongly indicates they are an unsuitable instrument for temporary investment by municipalities.

Another thought: Perhaps the broad range of investment powers in K.S.A. 12-1675 et seq. provide municipalities with adequate investing options, making K.S.A. 10-131 an unnecessary statute?

I trust you will find this research helpful as you proceed with your bill. Please feel free to contact me if you wish further discussion and/or research on this matter.

Senate F+I
3/14/96
Attachment #2

STATE OF KANSAS

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Sally Thompson
TREASURER

TELEPHONE
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Testimony in Support of House Bill No. 2683
Senate Financial Institutions and Insurance Committee
Thursday, March 14, 1996
Rogers L. Brazier, Jr.
Office of the State Treasurer

Mr. Chairman, members of the committee,

Thank you for the opportunity to appear before the committee in support of House Bill 2683. My name is Rogers Brazier. I am employed by the office of the State Treasurer, Sally Thompson.

Two years ago the legislature passed Senate Bill 393, completely overhauling the state's unclaimed property law. The purpose of House Bill 2683 is to provide some relief to holders by reducing potentially unnecessary paperwork as well as reducing the labor intensive process performed by staff to audit and code holder reports.

The proposed amendments are as follows:

Section 1. Amendment of K.S.A. 58-3935 relates to the notice requirements imposed on holders prior to assessment of a dormancy fee.

The amendment calls for an increase from $25 to $50 the value threshold which triggers mandatory notice requirements that the holder must comply with prior to imposing a dormancy fee against property which is payable or distributable.

This amendment was requested by the Kansas Credit Union Association during the hearing before the House committee.

Section 2. Amendment of KSA 58-3939 to reduce the number of occasions when a demand or savings account at a bank or financial organization must be presumed abandoned.

Senate FI+I
3/14/96
attachment #3

Under the current law, an account which is "presumed abandoned" triggers certain notice, reporting and remittance requirements that must be complied with by "holders" (in this case the banks and financial organizations). For example, if I opened a savings account to help pay for my daughter's college tuition, and did nothing with the account for five years except receive my monthly statements, that account could be presumed abandoned and turned over to the state as unclaimed property if I did not respond to a due diligence notification from the financial organization, despite the fact that regular correspondence to me was not returned to the financial organization.

It is our position that as long as regular correspondence has not been returned to the sender, we should not assume the account to be abandoned.

The office has received numerous calls and letters from banks and other financial institutions expressing support for this amendment. This amendment will reduce the number of accounts for which notice, reporting and remittance is required.

Section 3. Amendment of KSA 58-3950 to increase from $25 to $50 the dollar value of property presumed abandoned for which holders (generally, business entities) must provide mandatory notice to owners as well as report detailed information to the State Treasurer.

Generally, for property valued at $25 or more, holders complete owner notification requirements and then report to the State Treasurer specific detailed information on property presumed abandoned. For similar property valued at less than $25, the holder is allowed to report in the aggregate, which alleviates the notification requirements and the reporting of detailed information.

The proposed amendments would raise the dollar limit to $50 or more providing significant reporting and notification relief to all holders. According to the National Association of Unclaimed Property Administrators, 29 states currently use aggregate dollar amounts of $50 or more.

Section 4. Amendment of KSA 58-3951 has two parts:

> First, to increase the dollar value of abandoned property for which the State Treasurer must advertise owner information. The proposed increase from $25 to $50 or more parallels the proposed increases to dollar amounts described in section 2, above.
>
> Second, to eliminate the requirement of current law that the office of the State Treasurer annually advertise in a newspaper generally circulating in this state, information concerning unclaimed property remitted in the previous year.

The State Treasurer has implemented more complete and less costly ways of advertising names of apparent owners. The State Treasurer provides each county clerk and county treasurer a listing of apparent owners with an address in Kansas, not just the property remitted in the previous year. The listings are updated twice a year, in January and July after the November and May reporting cycles. In addition, electronic data files of all apparent owners are provided to Kansas INK on a monthly basis.

The proposed amendment to KSA 58-3951 will give the State Treasurer discretion to determine the manner in which annual advertisement is made.

Summary

In summary, the proposed amendments to the uniform unclaimed property act found in House Bill 2683 will benefit holders by reducing the overall burden of required notification and reporting paperwork, will increase the efficiency of auditing and coding holder reports, will enhance the ability of unclaimed property staff to process higher volumes of holder reports, and provide more flexibility for administration of the program.

I've attached two pieces of information for your review: the first is statistical information regarding the unclaimed property program and the other represents the number of properties published compared to the number of properties available in each county.

I would be happy to answer questions.

Kansas
Credit
Union
Association

Testimony on HB 2683
AN ACT concerning unclaimed property
Presented to the
Senate Financial Institutions and Insurance Committee
March 14, 1996

Thank you Mr. Chairman and members of the Committee:

I am Danielle Noe and I am here on behalf of the Kansas Credit Union Association and its 160 member credit unions. Our members serve over 600,000 Kansans.

We are here today to support HB 2683 relating to unclaimed property.

In 1979 the Disposition of Unclaimed Property Act was enacted to supersede the state escheat law. Some of you will recall that the Unclaimed Property Act was once again rewritten during the 1994 session as SB 393. The Kansas Credit Union Association has always thought of this Act as pro-consumer legislation.

HB 2683 was recommended due to concerns that have been raised since the 1994 changes.

The first change (page 2, line 14) relates to how a financial institution determines when property is abandoned. Beginning with the 1979 Act, financial institutions have been allowed to use returned mail as an indication that property may be unclaimed. Conversely, it was presumed that if regular correspondence was not returned to the sender, the property was presumed to be claimed.

During the revision of the unclaimed property act two years ago this provision was not included. HB 2683 would put back into the Act a provision

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Senate FI&I
3/14/96
Attachment # 4

allowing financial institutions to use return mail as an indication of the status of the property.

The current act allows financial institutions to use other account activity as a presumption that the dormant account is also claimed. Practically speaking, our members' data systems will not cross reference accounts in that manner. Essentially, our members must first find the dormant accounts that fit the definition of unclaimed property. Then they must manually search all of their accounts to determine whether or not the owner of the unclaimed account has another account which is not a dormant account.

If our members were allowed to use returned mail as a way to determine whether an account is claimed, it would not only simplify the process but it would also ensure that only the property which is truly unclaimed escheats to the state.

The second change in HB 2683 (section 2) relates to the information which must be reported to the treasurer's office. The change will increase to $50 the value of property which must be reported individually to the state. The current statute says that if the unclaimed property (with some exceptions) has a value of less than $25 it can be reported in the aggregate. We feel that this change will reduce the amount of time it takes our members to fill out the forms required by this Act.

The third change in HB 2683 (page 3, line 19) relates to those account owners which must be given additional notice that their account is about to be subject to custody of the treasurer. This change would also increase to $50 the value of property which requires this notice. Again, we believe that this change will reduce the time that our members must spend reviewing their dormant accounts.

The House made one amendment at our request. The amendment to K.S.A. 58-3935, relates to the notice requirements before a financial institution can impose a dormancy fee. When a member opens an account, they contract at that time to pay a dormancy charge. Currently, this section requires a second notice prior to the imposition of a charge when the dormant account has a value of $25 or more. This change would increase the value to $50. This amendment will simply provide consistency within the act because of the increase in the value of property which requires additional notice and information under the Act.

Mr. Chairman, the changes in HB 2683 are offered in an attempt to simplify the procedures required under the Unclaimed Property Act. We ask that you act favorably on HB 2683.

Matthew S. Goddard, Vice President

700 S. Kansas Ave., Suite 512
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To: Senate Financial Institutions and Insurance Committee

From: Matthew Goddard
Heartland Community Bankers Association

Date: March 14, 1996

Re: House Bill No. 2683

The Heartland Community Bankers Association appreciates the opportunity to appear before the Senate Committee on Financial Institutions and Insurance in support of HB 2683.

This bill would restore a provision to the state statute concerning unclaimed funds that was omitted when it was rewritten by the legislature in 1994. At present, if a customer opens a savings account with the intent of earning interest from the initial deposit, that account is presumed abandoned if there is no account activity for a five year period. With passage of HB 2683, a demand or savings account would not be presumed abandoned if mail to the account owner has not been returned to sender. The bill also raises the threshold amount from $25 to $50 for a variety of reporting requirements.

The primary burden imposed on financial institutions by unclaimed property is one of simple reporting. Our membership tries to find the owners of dormant accounts. As long as the account owner is receiving correspondence about their account, regardless of any account activity, we see little justification in assuming abandonment and surrendering their funds to the state.

For the customer, HB 2683 helps ensure that their funds are available at their local financial institution even though there may not have been account activity in quite some time. It can be a frustrating experience for a customer when they try to make a withdraw only to be told their money is no longer at the institution.

We respectfully request that the Senate Committee on Financial Institutions and Insurance recommend HB 2683 for passage.

Thank you.

Senate FI&I
3/14/96
Attachment #5