Approved: 1-30-01
Date

MINUTES OF THE SENATE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE.

The meeting was called to order by Chairperson Sandy Praeger at 9:30 a.m. on January 24, 2001 in Room 234-N of the Capitol.

All members were present except:

Committee staff present: Dr. Bill Wolff, Kansas Legislative Research Department
Ken Wilke, Office of the Revisor of Statutes
JoAnn Bunten, Committee Secretary

Conferees appearing before the committee:

Franklin W. Nelson, State Bank Commissioner
Judi Stork, Div. of Banks and Trust Companies, Deputy Bank Commissioner
Kevin Glendening, Div. of Consumer and Mortgage Lending, Deputy Commissioner
Sonya Allen, General Counsel, State Bank Commissioner's Office

Others attending: See attached list.

Introduction of bills

The Chair requested introduction of a bill relating to mental health parity. Senator Feleciano made a motion that the Committee introduce the proposed legislation, seconded by Senator Teichman. The motion carried.

Office of the State Bank Commissioner

The Committee was briefed on the various duties and responsibilities of the State Bank Commissioner's office by Franklin W. Nelson, State Bank Commissioner; Judi Stork, Division of Banks and Trust Companies, Deputy Bank Commissioner; Kevin Glendening, Division of Consumer and Mortgage Lending, Deputy Commissioner; and Sonya Allen, General Counsel, State Bank Commissioner's Office. (Attachment 1)

Judi Stork requested introduction of two bills relating to banking that would create a trust company for limited purpose and authorization of special orders of the Bank Commissioner. Senator Salmans made a motion that the Committee introduce the proposed legislation, seconded by Senator Teichman. The motion carried.

Adjournment

The meeting was adjourned at 10:30 a.m. The next meeting of the Committee is scheduled for January 25, 2001.

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: 1-24-01

NAME	REPRESENTING
Judi Stork	OSBC
Sonya Allen	OSBC
Franklin W. Nelson	OSBC
Kevin Glendening	OSBC
John Milburn	AP
Carol [illegible]	HWS
Nancy Shaughnessy	Federico Consulting
Matt Goddard	HCBA
Chuck Stones	KBA
Kathy Olsen	KBA
Jin Liu	DOB
John Peterson	Ks Governmental Consulting
Harrie Ann Lower	KAHP
Roger Franzke	KGC

STATE OF KANSAS
BILL GRAVES
GOVERNOR

Franklin W. Nelson
Bank Commissioner

Judi M. Stork
Deputy Bank Commissioner

Sonya L. Allen
General Counsel

Kevin C. Glendening
Deputy Commissioner
Consumer and Mortgage Lending

OFFICE OF THE
STATE BANK COMMISSIONER

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

January 24, 2001

Madame Chair and Members of the Committee:

My name is Franklin W. Nelson. I was appointed Bank Commissioner by Governor Graves and have served in that capacity since December 20, 1999. I was in banking for 26 years as a chief executive officer and bank owner.

I am pleased to be here today to speak before this committee concerning the Office of the State Bank Commissioner (OSBC). Over the years, our agency has enjoyed a good working relationship with this committee and I look forward to being of service to you, Madame Chair, and to each member of this committee. If my staff or I may be of assistance to you or your constituents, please do not hesitate to contact us. Let us be a resource to you. We may not have all of the answers that you seek, but we shall strive diligently to provide you with meaningful and accurate information. Attached to my testimony is a list of key agency personnel, including our telephone number and e-mail addresses.

Senate Financial Inst. & Insurance
Date: 1-24-01
Attachment No. 1

.is agency was first formed 110 years ago, in 1891, to oversee the numerous private banks then in existence Kansas. Today, the OSBC regulates **270** state-chartered banks, **11** trust companies, **52** trust departments in state banks, **25** money transmitter companies, over **353** mortgage lenders and brokers, **292** licensed supervised lenders with **703** licensed locations, **5** credit service organizations, and over **6000** filers who extend consumer credit. I would like to point out that we are a fully fee funded agency, with all of our revenues coming from these regulated entities. We have seven field offices located throughout the state, with our largest offices in Overland Park, Wichita, and Topeka, and our smallest in Dodge City. All examination staff, including trust and consumer credit examiners, work out of these field offices. In Topeka, we maintain a review examination staff, a legal department with three attorneys, an administrative unit, information tech staff, and a support staff.

As most of you are aware, the consolidation of the Office of the Consumer Credit Commissioner into the Office of the State Bank Commissioner occurred approximately 18 months ago, on July 1, 1999. This consolidation was a common sense approach to regulation of two similar industries. The consolidation resulted in the separation of duties into two divisions within the OSBC. They are the Division of Banks and Trust Companies, headed up by Deputy Bank Commissioner Judi Stork; and the Division of Consumer and Mortgage Lending, headed up by Deputy Commissioner Kevin Glendening. In a moment, I will ask each Deputy Commissioner to give a short informative presentation regarding their respective division. Also, our General Counsel, Sonya Allen, will give you an informative overview of a complicated subject, that being the Gramm-Leach-Bliley Act, also now known by the acronym GLBA - pronounced "glubba".

Right now, I would like to spend a little time talking about my goals as Commissioner and the future direction of this agency.

I see the future role of the Office of the State Bank Commissioner as multi-faceted. First, I see our role as an advocate for consumers, to ensure they are protected from unsafe or unscrupulous practices by financial service

oviders. We regularly examine state-chartered banks to ensure they remain a safe place for consumers deposit their money. We also have taken major steps to implement improved supervision over mortgage brokers and lenders, and suppliers of consumer credit, by enforcing the laws governing those transactions. We intend to expand our supervision and enforcement role in the consumer area as we acquire additional resources.

Second, our role is as an educator of consumers of financial services. We accomplish this through one-on-one consumer assistance, grants to consumer education groups, and the availability of a toll-free consumer hotline. We are also an educator of the entities we regulate. Through the examination process, part of our objective is to promote a better understanding of, and compliance with, applicable laws and regulations.

Third, our role is to ensure the viability of the state banking system in Kansas. I firmly believe we need to ensure the state bank charter is the charter of choice for new banking groups who enter the marketplace.

In order to understand the importance of the state charter, I would like to provide you with a brief overview of the dual banking system. It is described as a "dual system" because of its two parallel systems of bank chartering, regulation, and supervision. Both the federal government and individual states issue bank charters and examine those banks for the benefit of their citizens. States have been regulating banks since before the creation of an independent United States. When Congress created the national bank charter in 1863, it created the Office of the Comptroller of the Currency, commonly known as the OCC. The OCC issues charters and regulates national banks. State bank supervisors issue charters and are the primary regulators of state banks. The Federal Deposit Insurance Corporation (FDIC) insures deposits in both state and national banks. State banks also receive federal supervisory oversight from either the FDIC or the Federal Reserve System. The existence of state and national charters provides a creative tension that exists nowhere else in the world of bank supervision. The choice of

harters encourages innovation in bank powers and in regulatory techniques, and acts as a check and balance bank regulators. Maintaining state-chartered banks means Kansas maintains control of the practices of these banks, and the Kansas Legislature can tailor laws to suit what is best for Kansas citizens. You will find our 2001 legislative initiatives include proposals for some minor enhancements of the state bank charter, which will grant additional parity for Kansas state chartered banks.

I believe it is essential to the viability of the state charter in this state for the OSBC and the legislature to explore more efficient methods for Kansas to address the rapid and continuing change in the financial services' world. I believe OSBC's regulatory efforts and future legislative efforts must go beyond a "reactive response" to the ever-changing financial services environment in our state and national economy. What I mean by "reactive response" is an ongoing situation whereby, as financial services innovation occurs, Kansas only reacts and responds after the fact by saying, "me too." I continue to advocate a conservative and studied approach as to the best way to address change and innovation. However, I firmly believe that we should enhance the state bank charter and embrace creative tools that allow state chartered banks to help grow the Kansas economy and generate jobs, products, and services.

I look forward to working with all of you throughout this session and the coming years.

At this time I would like to introduce Judi Stork, Deputy Bank Commissioner; who will continue this presentation with an overview of the Division of Banking.

DIVISION OF BANKS AND TRUST COMPANIES

The Division of Banking has the statutory duty to examine banks and trust companies once every 18-month period. We accomplish compliance with this statute by doing alternating and/or joint examinations with the Federal Reserve Bank and the Federal Deposit Insurance Corporation. We have 56 employees within this division - 47 of those individuals are

examiners. These examiners review all aspects of our institutions and provide a written report to our office. report is reviewed by staff and forwarded to the Commissioner for final review and signature. The report is then provided to the bank or trust company. A rating is assigned to each of our banks and trust companies. We assess the condition of the **C**apital, **A**ssets, **M**anagement, **E**arnings, **L**iquidity, and **S**ensitivity to Market Risk of each bank. We then rate each component on a scale of one to five, with a one rating being the best and a five being the worst. The CAMELS rating is disclosed to each bank in their examination report.

To give you a better idea about the past and current condition of banks in Kansas, please note the chart below.

OSBC State Bank Examination Data Sheet - Year Ends

Year Ending	Not Rated	1	2	3	4	5	Total / 3-4-5
12-86	0	65	213	95	59	12	444 / 166
12-87	0	69	202	92	56	16	435 / 164
12-88	0	76	194	106	40	8	424 / 154
12-89	0	71	214	87	30	5	407 / 122
12-90	0	72	199	81	40	2	394 / 123
12-91	0	62	219	69	25	4	379 / 98
12-92	0	68	214	64	18	1	365 / 83
12-93	0	97	197	47	5	4	350 / 56
12-94	0	121	181	24	9	1	336 / 34
12-95	0	138	158	17	2	0	316 / 19
12-96	0	144	134	14	1	0	293 / 15
12-97	0	171	111	5	1	0	288 / 6
12-98	2	167	108	3	1	0	281/ 4
12-99	2	154	117	4	2	0	279 / 6
12-00	2	146	111	7	4	0	270 / 11
1/12/01	2	146	111	7	4	0	270 / 11

You can see from the chart that we consider only eleven of our banks to be problem institutions. This number is substantially lower that in 1986 when approximately 37% of our banks were on the problem bank list.

e trust side, we use a similar rating system. The ratings for year-end 2000 are as follows:

Week Period	Not Rated	1	2	3	4	5	Total Active Departments
12-31-2000	2	7	1	1	0	0	11

Again, you can see the condition of the trust companies is considered favorable.

Our office also reviews and approves various banking and trust company applications. We have a nine-member banking board - six bankers, three public interest members - which meet monthly in our office. They review and approve new charters, branches, name changes, relocations, etc. The Commissioner approves mergers, acquisitions, trust powers, etc.

I would like to touch briefly upon the special orders that were issued, pursuant to K.S.A. 9-1715, during the year 2000. As many of you know, the Bank Commissioner has the authority under this statute to grant powers to state banks, which they could exercise if they were a national bank. This power can be granted to the state bank if the state bank is at a competitive disadvantage to the national bank. During 2000, the Commissioner issued three special orders.

Special 2000-1: Financial Subsidiaries

On November 12, 1999, President Clinton signed into law the Gramm-Leach-Bliley Act (P.L. 106-102), updating U.S. financial services laws and breaking down the barriers between commercial banks, securities firms, and insurance companies. A key provision in this Federal law granted national banks the authority to form or hold an interest in "financial subsidiaries." This provision became effective on March 11, 2000. The authority to form financial subsidiaries provided national banks with new opportunities to engage in a broader array of financial services and to affiliate with nonbank entities like securities firms and insurance companies. Numerous state-chartered banks contacted this office inquiring about the issuance of a Special Order to grant parity between state and national banks with regard to financial subsidiary formation. Current Kansas statutes did not allow state banks to form financial subsidiaries.

d on these facts, it was determined that Special Order 2000-1 should be issued, allowing state banks to form an interest in financial subsidiaries to engage in certain specified activities. Any bank desiring to form or hold an interest in a financial subsidiary must provide certain information to the Commissioner and receive prior approval to engage in the activity.

Special Order 2000-2: Investment in Obligations of Government Sponsored Enterprises

Federal law authorizes national banks to invest in obligations of government sponsored enterprises without limitation. Many state-chartered banks were operating under the assumption that there was no limit in Kansas law on such investments. Upon further review of Kansas statutes and various Attorney General's Opinions, it was discovered that current Kansas statutes do not clearly allow state banks to make such investments without limitation.

It was determined that Special Order 2000-2 should be issued in order to ensure parity and promote competitive equality between Kansas state and national banks. The Order provides authority for state banks to invest without limit in obligations of the government sponsored enterprises set out in the Order.

Special Order 2000-3: Minority Investment in a Bulk Mailing Operation (Bank-Specific Order)

Federal law authorizes national banks to make a minority investment in an entity that engages in activities a national bank could engage in directly, provided certain safety and soundness criteria are met. A Kansas bank requested permission to acquire a minority interest in stock of a Kansas corporation engaged in postal substation activities. The bank planned to use this company to perform bulk mailing services on behalf of bank customers and also to provide those services to non-bank customers.

Upon review, it was determined that the circumstances warranted the issuance of Special Order 2000-3, which allows the bank to own a minority interest in a corporation that performs bulk mailing services.

k you for the opportunity to share these comments. I do have two bill introductions today. I am also ha[illegible] answer any questions you may have.

At this time I would like to introduce Kevin Glendening, the Deputy Commissioner for the Consumer and Mortgage Lending Division.

DIVISION OF CONSUMER AND MORTGAGE LENDING

HISTORY

In July 1999, the Office of the Consumer Credit Commissioner was merged into the OSBC. The legislation created the present structure of the OSBC with a Bank Commissioner, a Deputy Commissioner for the banking division, and a Deputy Commissioner for the newly created consumer and mortgage lending (CML) division, who also serves as the Administrator of the Kansas Uniform Consumer Credit Code (UCCC).

WORK OF THE DIVISION

The CML division licenses and regulates the activities of several distinct trades including mortgage brokers and lenders, consumer finance companies, and payday lenders. Through the administration of the UCCC, we also impact a much broader range of businesses that engage in consumer credit transactions in this state. The nature of both consumer lending and mortgage lending have substantially changed over the past decade or so. Some factors that have contributed to that change include the acceptance by capital markets of more relaxed underwriting standards spawning the so called sub-prime market; growth in home equity lending for debt consolidation purposes; and, the proliferation of companies beyond traditional banks offering credit products to consumers.

At the time of the merger in 1999, the enforcement powers associated with the consumer and mortgage lending areas were also strengthened to combat predatory lending activities. Those enforcement tools include criminal penalties and monetary fines; the ability to issue subpoenas for witnesses and records to investigate violations of the UCCC; and, to

int a special prosecutor at the request of either the Attorney General or a county or district attorney to prose ; assist in the prosecution of those violations.

As you might imagine, with the large number of companies who in one form or another fall under the oversight of CML division, we have our work cut out for us. In calendar year 2000, we conducted on-site examinations of 94 companies which resulted in refunds to consumers of approximately $63,000; we received 670 consumer inquiries and complaints by way of telephone calls and 100 written consumer complaints; and, we initiated administrative actions against individuals and companies at an average rate of more than one per week. These actions resulted in assessed fines of nearly $75,000, and refunds, revised loan contract terms, and other issues benefiting those consumers by nearly $300,000.

GOALS AND OBJECTIVES

First and foremost, our goal is to protect consumers from unfair and deceptive practices used by some lenders and other suppliers of consumer credit. We want to facilitate consumers in making more informed choices about credit. In addition, we seek to encourage the development of fair and economically sound credit practices which foster competition and allow consumers to obtain credit at reasonable cost.

To achieve these goals, three objectives are extremely important: First, equal and aggressive enforcement of the laws through examinations of licensed companies, and actively responding to predatory or unethical business practices brought to our attention by consumer inquiries and complaints. Second, sponsoring consumer education initiatives that stress fundamentals of personal debt management, wise use of credit, and the importance of being an informed consumer in evaluating credit choices. Third, educating both credit providers and consumers on restrictions and consumer rights embodied in our state's consumer and mortgage lending laws.

Over the past year, we've made some progress in meeting those objectives. We are working with several nonprofit consumer counseling groups in the state to develop free seminars and informational materials targeted to those

umers who desperately need education in the credit fundamentals I just spoke about. Also, as I mentioned,
taking a strong position, to the extent staff limitations permit, in enforcing the laws against those companies and individuals who attempt to ignore them. Having said that, it is also clear that a great deal of work remains to be done. A key factor to achieving these goals and objectives is adequate staffing of the CML division. As the Commissioner pointed out in his comments, we hope to address that issue with the legislature later this session.

At this time, I would like to introduce Sonya Allen. Sonya Allen is the General Counsel for the department.

GRAMM-LEACH-BLILEY ACT

Thank you for the opportunity to appear before you today. I have been given the formidable task of explaining hundreds of pages of complex federal legislation in five minutes or less. This legislation is called the Gramm-Leach-Bliley Act of 1999, and is commonly referred to as "financial modernization." Attached to our testimony you will find a very brief overview that was prepared to touch on the highlights of the Act, and to explain some key terms needed to understand it. There are numerous other summaries prepared by various organizations, individuals, and groups that we can make available to you, if you so desire. I believe that Dr. Wolff of the Legislative Research Department prepared a summary of the Act last year.

One resource that is available online was prepared by the Conference of State Bank Supervisors, of which we are a member. CSBS has the Act and a summary on its web site, at http://www.csbs.org/legreg/html.

Right now, I'd like to walk you through the attached summary and touch on some of the key points.

Madame Chair, that concludes our testimony. I will turn this presentation over to the Commissioner for questions.

Terminology

OSBC: The Office of the State Bank Commissioner.
That's us! Our office is part of the executive branch of state government. We are responsible for chartering and supervising state banks in Kansas. Our office also charters free-standing trust companies, and licenses and regulates money transmitters, mortgage lenders and brokers, supervised lenders, and other entities extending consumer credit who operate in this state.

OCC: The Office of the Comptroller of the Currency.
The OCC is a regulatory body within the Treasury department that issues national bank charters, and is responsible for regulation and supervision of national banks.

OTS: The Office of Thrift Supervision.
The OTS is a regulatory body within the Treasury department that issues national thrift charters (i.e., savings and loans, savings banks), and is responsible for their supervision and regulation.

FRB, or "The Fed": The Federal Reserve System.
The FRB is a central monetary authority for the U.S., created by the Federal Reserve Act of 1913, which consists of 12 district banks. The Federal Reserve Board of Governors in Washington, D.C. exercises overall control over the nationwide operations of the system. Kansas is part of the 10th Federal Reserve District, and our district bank is located in Kansas City, MO.

FDIC: The Federal Deposit Insurance Corporation.
The FDIC is an agency of the Federal government established in 1933 to provide insurance protection, up to statutory limits, for depositors at FDIC member institutions.

The Dual Banking System: The Dual Banking System is a U.S. system of chartering, regulating and supervising banks. Both the federal government and individual states issue bank charters and examine financial institutions for the benefit of their citizens.

GLBA, or "Glubba": The Gramm-Leach-Bliley Act of 1999.
GLBA is the federal legislation also referred to as "financial modernization," which was signed into law in November of 1999. GLBA updates financial services laws and breaks down the barriers between commercial banks, securities firms, and insurance companies.

Financial Modernization Overview: The Gramm-Leach-Bliley Act of 1999
Summary of Key Bank-related Provisions

The Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338, (GLBA) was signed by the President and enacted into law on November 12, 1999. The GLBA does three fundamental things:

1. It repeals key provisions of the 66-year old Glass Steagall Act to permit commercial banks to affiliate with investment banks.
2. It substantially modifies the 43-year old Bank Holding Company Act of 1956 to permit companies that own commercial banks to engage in any type of financial activity, through a new entity called a "financial holding company".
3. It allows subsidiaries of national banks to engage in a broader range of financial activities that are not permitted for the national banks themselves, through a new entity called a "financial subsidiary".

Some of the key concepts and provisions in the GLBA include the following:

I. Financial Holding Companies.

A financial holding company ("FHC") is simply a bank holding company that has elected to become a "financial holding company" pursuant to the GLBA. To be an FHC, the bank holding company must satisfy and continue to satisfy new regulatory requirements. FHCs are supervised by the Federal Reserve. A bank holding company may elect to become a financial holding company in order to engage in the broad new range of financial activities permitted under GLBA.

GLBA authorizes an FHC and its affiliates (meaning FHC subs that are not banks) to engage in activities that are:
Financial in nature;
Incidental to such financial activity; or
Nonfinancial, but complementary to financial activities.

Laundry list of activities that are "financial in nature" include:
Lending, exchanging, transferring, investing for others, or safeguarding money or securities;
All insurance underwriting and sales (brokerage) activities;
Investment or economic advisory services;
Securitizations;
All securities underwriting and dealing activities;
All "closely related to banking" activities previously approved for bank holding companies by the Federal Reserve Board under section 4(c) (8) of the Bank Holding Company Act;
Certain products offered overseas, such as travel agency services;
Merchant banking/equity investment activities.

Activities that are "incidental to financial activities":
The Federal Reserve Board, in consultation with the Treasury Department, is authorized to allow banking organizations to engage in other financial activities that are not in the enumerated "financial in nature" list, if they deem the activity to be "incidental to" a financial activity. In making this determination, they are to consider:
•Changes or reasonable expected changes in the marketplace in which the banking organization competes or the technology for delivering financial services; and
•Whether the proposed activity is necessary or appropriate to allow an FHC to:
→Compete effectively with any company seeking to provide financial services;
→Efficiently deliver information and services that are financial in nature through the use of technology, including applications involving systems for data transmission or financial transactions; and
→Offer customers any available or emerging technological means for using financial services or for the document imaging of data.

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"Complementary" Nonfinancial Activities:
The Federal Reserve Board has authority to allow FHCs to engage in certain nonfinancial activities if they determine that the activity:
•Is complementary to a financial activity; and
•Does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally.

II. Financial Subsidiaries.

A financial subsidiary is a new type of subsidiary authorized for national banks by GLBA. Financial subsidiaries can engage in most of the nonbanking activities that are deemed to be "financial in nature" or "incidental to a financial activity". These subsidiaries must be controlled by one or more depository institutions. "Control" is primarily defined as owning 25% or more of the shares of the company. Some of the activities that a financial subsidiary cannot engage in include underwriting of insurance, engaging in real estate development, or engaging in merchant banking (venture capital-type) activities. A national bank seeking to have a financial subsidiary, and each of its depository institution affiliates, must meet certain safety and soundness standards. In addition, the total assets of all of a national bank's financial subsidiaries must not exceed 45% of the parent bank's total assets or $50 billion, whichever is less. Equity investments in financial subsidiaries, including retained earnings, must be deducted from the parent bank's capital.

III. Unitary Thrift Holding Companies.

While GLBA substantially expands the ability of a bank to affiliate with any financial company, it also confirms the longstanding prohibition on a bank affiliating with a commercial company. Prior to GLBA, there was a type of vehicle called a "unitary thrift holding company", which allowed a commercial company to acquire a thrift institution. The Act contains a retroactive effective date on and after which such acquisitions are no longer allowed, which is May 4, 1999. Any commercial holding companies which were unitary thrift holding companies on May 4, 1999, were "grandfathered" under the Act.

IV. Federal Home Loan Bank System Reforms.

In general, GLBA made it easier to join the Federal Home Loan Bank System, (FHLB) by waiving the membership requirement that 10% of a bank's assets be invested in residential mortgage loans for institutions with $500 million or less in assets, and increased the borrowing capacity of depository institutions who are members of the FHLB by expanding the types of eligible collateral for FHLB advances. These changes will be extremely beneficial to small community banks.

V. Privacy.

The GLBA privacy provisions expand a customer's ability to protect the privacy of information provided to any kind of financial entity, including banks, securities firms, insurance companies, thrifts and credit unions. The Act attempts to strike a balance between personal privacy protections, and the legitimate needs of financial institutions to share information, especially among affiliates. The privacy provisions are complex, but four main requirements are imposed on a financial institution. A financial institution must:
•Establish and disclose annually its privacy policy (Tell customers what you do with their nonpublic personal information.)
•Afford customers the right to "opt out" of disclosures to non-affiliated third parties, subject to a number of exceptions. (A customer has no ability to opt-out of disclosures to affiliates.)
•Not disclose account information to third-party marketers.
•Abide by regulatory standards to protect confidentiality of consumer information.

Attached to this summary is additional detailed information prepared by the American Bankers Association on the privacy provisions of GLBA.

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VI. Community Reinvestment Act.

The GLBA requires that certain CRA requirements be met if companies and banks want to utilize the new powers in the Act. To become a financial holding company, all of the subsidiary depository institutions must have, and continue to have, a "satisfactory" CRA rating. If any subsidiary falls below the "satisfactory" level, there is an opportunity to cure the deficiencies. If the deficiencies are not cured within the allotted time, the FHC is prohibited from making new acquisitions or commencing new activities pursuant to the new powers granted under GLBA. Also included in this CRA section of GLBA were some regulatory relief measures for smaller community banks and thrifts, which included longer periods between CRA examinations. Finally, the Act included new requirements for public disclosure of CRA agreements between banking organizations and community groups or other private parties.

Sources:

"Financial Modernization: The Gramm-Leach-Bliley Act Summary"; American Bankers Association, November 12, 1999

"New Opportunities for Community Banks, Financial Modernization- The Gramm-Leach-Bliley Act, An ABA Workbook"; American Bankers Association, January 2000

"The Gramm-Leach-Bliley Financial Modernization Act of 1999: A Guide for the State System"; Conference of State Bank Supervisors, 1999

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APPENDIX D

DETAILED SUMMARY OF PRIVACY PROVISIONS

This appendix describes in more detail the Act's requirements regarding (A) the disclosure of nonpublic personal information of financial institution consumers; and (B) the prohibition on fraudulent access to such information.

A. Disclosure of Nonpublic Personal Information

As described below, a financial institution is subject to four new requirements regarding the nonpublic personal information of a consumer. For these purposes, a "consumer" means an individual who obtains financial products or services from a financial institution primarily for personal, family, or household purposes; it does not include any corporate entity or any individual or corporate business customer. "Nonpublic personal information" generally means personally identifiable financial information obtained by any means, other than publicly available information.

1. Annual Disclosure of Privacy Policy

The Act's first privacy obligation for financial institutions is the requirement to establish and disclose a privacy policy.

General requirement. A financial institution must clearly and conspicuously disclose to each of its consumers its policies and practices for the protection and disclosure of nonpublic personal information.

Contents of disclosure.[31] Among other things, the disclosure must include the categories of information that are collected and the financial institution's policy and practices regarding—

- Disclosure of nonpublic personal information to ***both*** nonaffiliated third parties ***and affiliates.***
- Disclosure of nonpublic personal information of persons who are no longer customers.
- Protection of the confidentiality and security of nonpublic personal information.

Timing and form of disclosure. The disclosure must be made at the beginning of a financial institution's relationship with the consumer, and at least once each year thereafter as long as the relationship with the consumer continues. The disclosure must be in writing, electronic form, or other form prescribed by implementing regulations.

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[31] The Act's provisions regarding the contents of the disclosure are both redundant and confusing. This confusion will likely be resolved by the implementing regulations.

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2. Customer "Opt-Out" of Disclosures to Third Parties

The Act's second basic privacy obligation for financial institutions is the requirement that a consumer be afforded the right to prevent the disclosure of nonpublic personal information to a nonaffiliated third party—commonly referred to as the right to "opt out."

General requirement. A financial institution may not disclose nonpublic personal information to a "nonaffiliated third party" unless—

- The financial institution clearly and conspicuously discloses to the consumer that such information may be disclosed to the third party;
- The consumer is given the opportunity to direct that the information not be disclosed to the third party (the right to "opt out"); and
- The consumer is given an explanation of how to exercise the opt-out.

The financial institution does *not* have to provide the right to opt out when the information is provided to an *affiliate,* as opposed to a nonaffiliated third party. In addition, "nonaffiliated third party" is defined as an entity that is not under common control with the financial institution; a "joint employee" is not a nonaffiliated third party. As a result, the opt-out need not be provided if the financial institution provides the information to its employee who happens also to be an employee of a nonaffiliated third party.

Timing and form of disclosure. The consumer must be given the right to opt out *before* nonpublic personal information is initially disclosed to a nonaffiliated third party. And as with the privacy policy disclosure, the opt-out disclosure must be in writing, electronic form, or other form prescribed by implementing regulations.

Limits on re-disclosure of information. A nonaffiliated third party that receives nonpublic personal information from a financial institution may not re-disclose that information to any other nonaffiliated third party, unless it would have been lawful for the financial institution to make that disclosure in the first instance. The Federal Trade Commission ("FTC") is provided the authority to enforce the privacy restrictions in the Act that apply to non-financial institutions, which includes the re-disclosure restrictions that apply to a nonaffiliated third party that is not a financial institution.

Exceptions. There are many important exceptions to the opt-out requirement, the most significant of which are listed in Attachment 1 attached to this Appendix. For example, the opt-out does not apply where a financial institution discloses information to a nonaffiliated third party to market the financial institution's own products. The opt-out also does not apply where the disclosure is made to market financial products or services offered pursuant to joint agreements between two or more financial institutions. Community banks, in particular, should be able to take advantage of this "joint agreement" exception when partnering with other financial companies to sell securities or insurance.

Other exceptions to the opt-out requirement are intended to address situations, among others, where: it would not be practical to provide the opt-out (*e.g.*, where the sharing is done to produce a consolidated customer statement from affiliated companies); an opt-out would not be expected by the consumer (*e.g.*, where the sharing is necessary to complete a transaction or service the customer's account); or the information sharing would serve an equally important public policy as protecting the customer's privacy (*e.g.*, to comply with a regulatory investigation). As a group, these exceptions address fundamental concerns that had been raised by the financial services industry concerning the practical problems associated with an opt-out.

1-16

3. Prohibition on Disclosure of Account Information

The Act's third privacy requirement for financial institutions is a prohibition: A financial institution may not disclose an account number "or similar form of access number or access code" for a credit card account, deposit account, or transaction account of a consumer to any nonaffiliated party for use in telemarketing, direct mail marketing, or other marketing through electronic mail to the consumer. There is only one statutory exception to the prohibition, which applies to disclosures to a credit bureau. However, additional exceptions may be established by regulation.[32]

This prohibition does not apply to disclosures to an affiliate. As a result, the Act does not prevent the use of an account number either in a financial institution's own marketing, or in the marketing of the financial institution's products by an affiliate.

4. Regulatory Standards to Protect Security and Confidentiality

The Act's fourth privacy requirement for financial institutions derives from a vague provision that "it is the policy of the Congress that each financial institution has an affirmative and continuing obligation to respect the privacy of its customers and to protect the security and confidentiality of those customers' nonpublic personal information." Although this provision is worded quite broadly, its actual effect is unclear because it is stated merely as a "policy of the Congress" and appears not to impose any specific restrictions.

A related provision does, however, require each financial institution regulator, "in furtherance of the policy," to establish appropriate "standards" relating to safeguards to (1) ensure the security and confidentiality of customer records; (2) protect against any anticipated threats to the security of such records; and (3) to protect against unauthorized access to such records that could result in substantial harm or inconvenience to the customer. These proposed standards seem directed toward the physical security and integrity of customer records, which appears to be considerably narrower than the subject matter of the "Congressional policy" that it purports to implement. Moreover, the use of the term "standards," rather than "rules or regulations," suggests that the regulatory agencies are to provide generalized guidance rather than detailed regulatory prescriptions.

5. Rulemaking and Enforcement

The Act requires the federal banking agencies, the National Credit Union Administration, the SEC, the Treasury Department, and the FTC *each* to prescribe regulations to implement the new privacy obligations for the institutions or persons under their respective jurisdictions. (As noted previously, the FTC will have jurisdiction over any institution or person that is subject to the privacy provisions but is not otherwise regulated as a "financial institution.") While these agencies are supposed to consult with one another to assure as much similarity in the regulations as possible, they may in fact issue quite different versions of such regulations—which would mean that quite different privacy rules could apply to different subsidiaries (*e.g.*, bank, insurance, and securities subsidiaries) owned by a single FHC. The agencies listed above, along with state insurance regulators, are to enforce the statute and implementing regulations.

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[32] The Act's legislative history indicates that, in granting regulatory exceptions, the regulators may consider it consistent with the purposes of the privacy provisions to permit the disclosure of customer account numbers in an encrypted form where the disclosure is expressly authorized by the customer and is necessary to service a transaction expressly authorized by the customer.

1-12

6. FCRA Rulemaking Authority

The Act eliminates the prohibition on the FTC and the federal banking agencies from issuing regulations under the FCRA, and in fact directs the federal banking agencies to jointly prescribe "such regulations as are necessary to carry out the purposes of the [FCRA]" (with the Federal Reserve prescribing regulations for bank holding companies). The Act also removes restrictions on the federal banking agencies' conducting examinations regarding FCRA compliance. Finally, the Act states that, with the exception of the provisions just mentioned, none of its new privacy provisions is intended to change the manner in which the FCRA applies to financial institutions. This means that FCRA requirements that had applied before the enactment of the Act, such as the disclosures required when a consumer's credit application information is shared with an affiliate, will continue to apply as before.

7. Relation Between Federal and State Laws

The Act generally provides that the new federal privacy provisions will preempt only those state laws that are inconsistent with the federal laws. The exception is that such preemption will not apply if the state law provides *greater* privacy protection than the federal law, as determined by the FTC.

B. Fraudulent Access to Financial Information

The final privacy provision in the Act applies not to financial institutions, but to any person who fraudulently obtains or causes the disclosure of customer information from a financial institution by fraudulent or deceptive means. The Act makes such fraudulent access a federal crime, punishable by up to five years' imprisonment. The Act also provides the FTC and financial regulatory agencies with administrative enforcement power. This provision in the Act is aimed squarely at the abusive practice of "pretext calling," in which someone misrepresents the identity of the person requesting the information or otherwise misleads an institution or customer into making an unwitting disclosure of customer information. Although the prohibition applies directly to the conduct of the persons who seek fraudulent access, the Act directs the financial regulatory agencies to revise existing regulations and guidelines to ensure that financial institutions under their jurisdiction have policies, procedures, and controls in place to prevent, deter, and detect fraudulent access to customer information.

1-18

APPENDIX D—ATTACHMENT 1

DISCLOSURES NOT SUBJECT TO "OPT-OUT" REQUIREMENT

A financial institution may make the following types of disclosures of nonpublic personal information of a consumer to a nonaffiliated third party ***without*** providing the consumer the right to "opt out" of the disclosure:

- **Marketing certain financial products.** Disclosures to perform services on behalf of the financial institution, *including*—
  - ➢ Marketing of the financial institution's own products or services, and
  - ➢ Marketing of financial products or services offered pursuant to joint agreements between two or more financial institutions.

These exceptions apply only if the financial institution fully discloses to the consumer the providing of the information to the third party, and the third party agrees by contract to maintain the confidentiality of the information. *Community banks, in particular, should be able to take advantage of the "joint agreement" exception when partnering with other financial companies to sell securities or insurance.*

- **Necessary for transaction.** Disclosures that are "necessary to effect, administer, or enforce a transaction"—
  - ➢ In connection with servicing or processing a financial product or service requested or authorized by the consumer.
  - ➢ In connection with maintaining or servicing the customer's account with the financial institution, or with another entity as part of a private label credit card program or other extension of credit on behalf of such entity.
  - ➢ In connection with a proposed or actual securitization, secondary market sale (including sales of servicing rights), or similar transaction related to a transaction of the consumer.
  - ➢ Requested or authorized by the consumer.

For purposes of these exceptions, "necessary to effect, administer, or enforce" is defined broadly to include disclosures that are required or are the "usual, appropriate, or acceptable method" to—

- ➢ Carry out a transaction, record or service or maintain the consumer's account, or administer benefits or claims related to a consumer transaction;
- ➢ Provide the consumer with a confirmation or other record of a transaction or information on the value of a financial service or product;
- ➢ Accrue bonuses associated with a transaction;
- ➢ Enforce the rights of the financial institution in carrying out a financial transaction;
- ➢ Engage in a range of activities related to providing insurance or reinsurance; or
- ➢ Provide authorization, settlement, billing, processing, clearing, transferring, reconciling, or collection of amounts charged, debited, or otherwise paid using a check, debit or credit card, or other payment means.

1-19

- **Consent.** Disclosures made with the consent or at the direction of the consumer.
- **Customer protection.** Disclosures to protect the confidentiality or security of the customer's information.
- **Antifraud.** Disclosures to protect against fraud, unauthorized transactions, etc.
- **Dispute resolution.** Disclosures for "required institutional risk control," or for resolving customer disputes or inquiries.
- **Beneficial or fiduciary interests.** Disclosures to persons holding a legal or beneficial interest relating to the consumer, or to persons acting in a fiduciary or representative capacity on behalf of the consumer.
- **Rating agencies.** Disclosures to provide information to rating agencies, insurance rate advisory organizations, guaranty funds or agencies, and persons assessing compliance with industry standards.
- **Attorneys, accountants, and auditors.** Disclosures to any of these service providers.
- **Law enforcement.** Disclosures to law enforcement agencies, other agencies, or self-regulatory organizations if specifically permitted or required under other provisions of law.
- **Public safety investigation.** Disclosure for an investigation involving public safety.
- **Credit bureaus.** Disclosures to a consumer reporting agency in accordance with the FCRA, or from a consumer report reported by a consumer reporting agency.
- **Sale or merger.** Disclosures made in connection with a proposed or actual sale or merger of all or a portion of a business, if the disclosure of the nonpublic personal information concerns solely consumers of such business or unit.
- **Legal requirements, judicial process, or regulatory compliance.** Disclosures to comply with federal, state, or local law; comply with regulatory investigations; respond to judicial process; or comply with examination or related requirements.
- **Regulatory exceptions.** In addition to these statutory exceptions, additional exceptions may be provided by regulation to permit other types of disclosures without the opt-out.

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OFFICE OF THE STATE BANK COMMISSIONER
700 Jackson, Suite 300
Topeka, Kansas 66603
785-296-2266
785-296-0168 FAX

Franklin W. Nelson
Bank Commissioner
franklin.nelson@state.ks.us

Judi M. Stork
Deputy Bank Commissioner
judi.stork@state.ks.us

Kevin C. Glendening
Deputy Commissioner- Consumer and Mortgage Lending
kevin.glendening@state.ks.us

Sonya Allen
General Counsel
sonya.allen@state.ks.us

Jenna Hall
Consumer Relations Officer
jenna.hall@state.ks.us

Kansas joins investigation of developer

By PAUL WENSKE
The Kansas City Star

Kansas banking officials have joined with Missouri and federal officials in investigating complaints against a Leawood contractor accused of building substandard homes and illegally soliciting mortgage business.

Kevin Glendening, head of the consumer and mortgage lending division of the Kansas bank commissioner's office, said Tuesday that his office was investigating complaints against Miller Enterprises.

The developer has built dozens of homes selling for $150,000 and above on both sides of the state line in metropolitan Kansas City.

A Johnson County District Court judge Friday issued a temporary restraining order against Miller Enterprises and a related company, Associated Finance Inc. The order prohibits them from soliciting mortgages in Kansas. A hearing on the order is scheduled for Oct. 23.

Glendening said the bank commissioner's office alleged that Miller Enterprises, owned by Jeffrey Miller, illegally operated as a mortgage company without a license.

"We're taking this action to further our investigation into the complaints that we have received," Glendening said Tuesday. He said the investigation was looking for any violations of the Kansas Mortgage Business Act and the state's consumer protection act.

Miller Enterprises is also under investigation by the Kansas attorney general's office and the U.S. Department of Housing and Urban Development. Those investigations turn on accusations of substandard home construction and predatory-lending complaints.

The developer's attorney and spokesman, R. Pete Smith, has denied any improprieties on the part of Miller Enterprises.

Smith was unavailable Tuesday, but he has in the past said the allegations stem from "a bandwagon of people who were told this was a way they could get out of paying their mortgages."

Investigators said they were reviewing allegations from homeowners that the developer increased the price they had to pay at closing. Some buyers said they were unable to keep up with their mortgage payments and ended up facing foreclosure proceedings.

The Kansas bank commissioner's office says, among other things, that Miller Enterprises improperly solicited mortgage business at www.maplewoodre.com.

To reach Paul Wenske, consumer affairs reporter, call (816) 234-4454 or send e-mail to pwenske@kcstar.com.

Senate approves increase in visas

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1-23

Lender to pay fine, issue refunds

Wyoming firm agrees to reimburse Kansas customers

By PAUL WENSKE
The Kansas City Star

A Wyoming payday loan company has agreed to pay a $10,000 fine to the state of Kansas and another $10,000 to Kansas customers who were charged illegal loan fees.

Wyoming Financial Lenders Inc. of Casper, which operates as Money Lenders, agreed to pay the fine and refunds as part of a settlement with the Consumer and Mortgage Lending Division of the Office of the Kansas Bank Commissioner.

Deputy Commissioner Kevin Glendening said the lending law violations were discovered during routine examinations of the company's loan shops in Dodge City and Garden City.

Company officials did not return telephone calls Thursday seeking comment.

Glendening said the company had skirted state limits on lending practices by inducing borrowers to enter multiple loan agreements, resulting in additional loan fees. The practice is prohibited in Kansas.

Rather than paying one fee on a $400 loan, for example, a borrower was induced into entering four loans of $100 each, which jacked up the amount of fees the borrower had to pay.

Glendening said the refunds involved about 300 loans made between November 1999 and March 2000. He said money from the $10,000 fine would be used to fund consumer education programs.

Glendening said splitting loans into multiple agreements had become more common in the industry, which includes 100 payday loan offices in Kansas. His office has two more cases pending.

Glendening said he might seek support in the state Legislature to strengthen payday loan laws. Kansas payday loan laws are strict now, he said, but he wants to ensure that predominantly working-class borrowers are not taken advantage of by multiple loan agreements.

Payday loan firms have sought to depict themselves as small businesses that fill a niche. A recent industry survey suggests that the majority of payday loan customers are satisfied.

Payday lenders typically make small loans to individuals for 30 days or fewer. Their loan fees can, over a year, amount to more than 240 percent interest.

Payday loan fees and charges are governed by the Kansas Uniform Consumer Credit Code. Consumers with concerns about consumer or mortgage lenders can call the consumer division of the Office of the Kansas Bank Commissioner at (877) 387-8523.

To reach Paul Wenske, consumer affairs writer, call (816) 234-4454 or send e-mail to pwenske@kcstar.com.

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Iowa firm renovating Radisson

Overland Park hotel to become a Holiday Inn

CITYSCAPE

JOYCE SMITH

Kinseth Hospitality Cos., a hotel development, ownership, management, renovation and construction company, is renovating the Radisson Hotel Overland Park at 8787 Reeder Road and will convert it into

served about 15,000 people month-

supplies. The stores also have a "Learning Center" where customers can access information on animal care.

America's Country Stores are a minimum of 7,200 square feet of retail space with 5,000 square feet of warehouse space. The Kansas City locations have not been selected. The company hopes to open nine area locations. Purina Mills, based in St. Louis, has 45 stores and plans to open 50 more by 2002.

BUSINESS DIGEST

Corporate taxes

Dozens of America's most profitable companies enjoyed tax-free years during the 1990s largely because of legal tax breaks, according to an independent study released Thursday.

The report by the nonprofit Institute on Taxation and Economic Policy found that 250 companies paid a tax rate of 20.1 percent in 1998, down from 22.9 percent just two years before. The federal income tax rate for corporations is supposed to be 35 percent...

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1-24

State banking regulators fine money lender for overcharging

GARDEN CITY (AP) — State regulators have fined a Garden City and Dodge City payday lender $10,000 for overcharging borrowers and violating the state's licensing law.

Wyoming Financial Lenders Inc., of Casper, Wyo., which operates as Money Lenders in Garden City and Dodge City, must also repay $10,000 to as many as 100 borrowers in addition to the fine, said Kevin Glendening, deputy commissioner of the Consumer and Mortgage Lending Division of the State Bank Commissioner.

The fine was paid this week, Glendening said, and the company has until mid-November to compensate consumers. It encompasses 300 loans made between November 1999 and March of this year.

Payday lenders make loans to people who need help making ends meet.

"Typically, it is someone who oftentimes they aren't making enough money at their job to handle expenses," Glendening said. "They need the money to make it to their next paycheck."

Most of the violations, uncovered last May during a routine examination, occurred in the Garden City office, he said.

Violations include boosting fees, such as when a customer comes in for a $400 loan and the lender makes four $100 loans to charge the maximum fees on each loan.

Another violation discovered was failure to properly disclose the terms of the loan or to alter its terms, Glendening said. Lenders are required to give the borrower a disclosure form, stating the amount borrowed and interest charged.

Money Lenders had either failed to state the interest charged or altered the figure listed on the disclosure form, Glendening said. The company also failed to disclose that it could collect returned check charges.

firm's failure to renew its license on time.

Personnel at Money Lenders' offices in Garden City and Dodge City referred calls to the administration office in Wyoming, and personnel there were unavailable for comment.

Money Lenders received its initial license to operate in Kansas in May 1999.

Glendening said his office has not had any problems with Financial Lenders Inc. in the past.

The $10,000 fine will be used for educational purposes such as consumer counseling and consumer education in schools.

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