

SUBJECT: Modifying minimum capital, exemption requirements of trust companies

COMMITTEE: Investments and Financial Services — committee substitute recommended

VOTE: 6 ayes — Parker, Longoria, Capriglione, Flynn, Landgraf, Stephenson
0 nays
1 absent — Pickett

WITNESSES: For — (*Registered, but did not testify:* John Heasley, Texas Bankers Association)
Against — None
On — (*Registered, but did not testify:* Bob Bacon and Everette Jobe, Texas Department of Banking)

BACKGROUND: The state’s trust companies are governed by Finance Code, Title 3, subtitle F.

Finance Code, sec. 182.008 stipulates that the banking commissioner cannot issue a charter to a trust company with less than \$1 million in restricted capital. According to sec. 184.101, the trust company must have at least 40 percent of its restricted capital invested in liquid assets, which are investments that are readily marketable and can be converted to cash within four business days.

Trust companies in Texas are considered insolvent if they meet one of several criteria outlined in sec. 181.002. For example, a company is insolvent if it has less than \$500,000 in equity capital as determined under regulatory accounting principles.

Finance Code, sec. 182.011 provides an exemption to these capital requirements for certain trust companies. To obtain an exemption, a trust company must file an application in writing with the Texas Department of

Banking, which may grant the exemption if it finds that the company does not conduct business with the public. The department may attach conditions and requirements to the exemption. Under sec. 182.013, the trust company must file an annual certification to maintain their exemption confirming that the trust company is in compliance with the exemption requirements. The certification is not valid unless acknowledged by the department.

Trust companies that were chartered before 1997 have maintained an exemption to these capital requirements through a grandfather clause in Finance Code, sec. 182.019.

Under sec. 182.015, an exempt trust company that is sold or transferred cannot maintain its exempt status.

DIGEST:

CSHB 3308 would modify several sections of Finance Code, Title 3, subtitle F related to minimum capital requirements for the state's trust companies and exemptions from these requirements.

Capital requirements. The banking commissioner would not be allowed to issue a charter to a trust company with a restricted capital of less than \$2 million. Unless granted an exemption by the banking commissioner, trust companies would be required to maintain an amount of liquid capital that was at least 50 percent the amount of its restricted capital.

A trust company would be considered insolvent if its equity capital, the amount by which the total assets of a trust company exceed its total liabilities, was 50 percent or less than the amount of its restricted capital.

Trust companies would have until September 1, 2020, to meet all of the bill's capital requirements. Trust companies would have until September 1, 2016, to meet the bill's 50 percent liquidity requirement. The bill would authorize the Finance Commission to adopt rules specifying a procedure for ratable increases in restricted capital and for deferrals and extensions of the requirements for a trust company acting in good faith.

Exempt status. Trust companies may qualify for exempt status if:

- the trust company had only family clients and transacted business only on their behalf;
- the trust company was wholly owned by family members;
- the trust company did not hold itself out to the general public as a corporate fiduciary for hire; and
- the trust company did not transact business with the general public.

The bill would define "family client" and "family member" and would allow the Finance Commission to further define in rule who could qualify as a family client.

Exempt trust companies would be required to file an annual certification that they are in compliance with the exemption requirements, in addition to a record of the trust company's condition and income. The bill would remove the requirement that a trust company's certification must bear an acknowledgement stamped by the department to be valid. The Texas Department of Banking could inspect the certification annually or otherwise as it deemed necessary.

The bill also would add a procedure for exempt trust companies to be sold or transferred without losing their exempt status. The person acquiring the trust company would be required to file a certification with the banking commissioner that the trust company would continue to comply with the exemption requirements. The Texas Department of Banking could examine or investigate the trust fund and the person acquiring it to verify the certification.

Examination of trust companies. CSHB 3308 no longer would allow the banking commissioner to delay an examination for up to six months. However, the commissioner could examine trust companies on a periodic basis as required by rule or policy. Current law already allows the commissioner to conduct examinations annually or as considered necessary to efficiently enforce the law while still safeguarding the interests of clients, creditors, and shareholders.

Trust companies would be required to file an annual statement of condition and income. The statement of condition and income would be

public record except for:

- statements of family trust companies exempted under the bill;
- statements of trust companies chartered before 1997; or
- portions of the statement that the banking commissioner designates confidential.

Grandfather clause. Trust companies that are exempt because they were chartered before 1997 would lose their exempt status either September 1, 2020, or when they are sold or transferred. Trust companies that lose their exempt status in this way could apply for an exempt status under the provisions contained in the bill.

Trust companies that are exempt because they were chartered before 1997 would have to increase their restricted capital to \$250,000 by September 1, 2020.

The bill would take effect September 1, 2015.

SUPPORTERS
SAY:

CSHB 3308 would better reflect the size, complexity, and growth of the modern banking industry in Texas by updating capital requirements for trust companies.

The amount of restricted capital set by the Department of Banking for each trust company serves as a benchmark to ensure the financial health of that company. This number is a quick guide that the state, the public, and the shareholders of the trust company can look at to gauge how much the trust company is supposed to own in equity capital and liquid assets. Some of the public trust companies in Texas now have hundreds of millions of dollars in assets. Requiring trust companies maintain at least \$500,000 in equity capital is no longer a realistic way to ensure the financial health of a trust company.

Changing the equity capital requirement to 50 percent of a trust company's restricted capital would be a more flexible approach to better guarantee the company's soundness. The 50 percent liquidity requirement and minimum \$2 million in restricted capital would make trust companies more financially secure. The bill also would modernize the exemption

process and would provide clear-cut guidelines for trust companies to qualify as exempt from capital and disclosure requirements.

It is unlikely that the new capital requirements would cause difficulties for many trust companies. The Texas Department of Banking has not chartered a trust with less than \$250,000 in capital since 1998. Of the 20 public trusts in the state of Texas, only three have less than \$2 million in capital, and none of the 20 currently would be unable to meet the liquidity requirement in the bill.

Ending the exemption by 2020 would give trust companies ample time to meet the new capital requirements. For exempt and non-exempt trust companies alike, the bill contains several clauses that allow and even encourage the Texas Banking Department and the Finance Commission to work with a struggling trust company.

The bill would allow for flexibility in the way the department conducted examinations of trust companies. While CSHB 3308 no longer would allow the commissioner to delay an examination, the commissioner could set a period longer or shorter than a calendar year for regular examinations. This would allow the Texas Department of Banking to base its examination schedule on the most efficient use of its resources.

**OPPONENTS
SAY:**

CSHB 3308 would establish capital requirements that smaller trust companies may have difficulty meeting. Trust companies often are used for estate planning and wealth management, so a trust company might be a shareholder or manager's largest, or in the case of an estate, only, pool of assets. The increased liquidity and restricted capital amount could prove to be a hardship for smaller trust companies.

For large trust companies, changing the liquidity requirement from 40 percent of restricted capital to 50 percent could make a big difference. Liquid assets tend to sacrifice either profitability or stability for the sake of liquidity. This bill could limit the ability of a trust company to participate in certain investment opportunities by requiring a large portion of the trust company's assets be invested in liquid assets.

NOTES:

The committee substitute differs from the bill as filed in that the substitute would not repeal Finance Code, sec. 184.101(b), which requires that a trust company have at least 40 percent of its restricted capital invested in liquid assets, and instead simply would amend that section.

The companion bill, SB 875 by Eltife, was passed by the Senate on April 9.