

BANKING
DEPARTMENT OF BANKING AND INSURANCE
DIVISION OF INSURANCE

Governmental Unit Deposit Protection

Eligible Collateral

Proposed Amendment: N.J.A.C. 3:1-4.13

Authorized By: Donald Bryan, Acting Commissioner, Department of Banking and Insurance

Authority: N.J.S.A. 17:1-8.1, 17:1-15(e) and 17:9-43

Calendar Reference: See Summary below for explanation of exception to calendar requirement

Proposal Number: PRN 2005-435

Submit comments by February 3, 2006 to:

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The agency proposal follows:

Summary

The Governmental Unit Deposit Protection Act (GUDPA), N.J.S.A. 17:9-41 et seq. provides that public depositories that have public funds on deposit in excess of the amount insured by the Federal Deposit Insurance Corporation (FDIC) shall maintain security for those deposits. Public depositories are State or Federally chartered banks, savings banks, or savings

and loan institutions with an office in New Jersey, the deposits of which are insured by the FDIC, and which hold public funds that are funds of a governmental unit.

A governmental unit means any county, municipality, school district or any other public body corporate and politic created or established under any law of this State by or on behalf of any one or more counties or municipalities, or any board, commission, department or agency of any of the foregoing having custody of public funds. Security for a governmental unit deposit is required to be in the form of eligible collateral.

N.J.S.A. 17:9-41 sets forth specific types of eligible collateral such as obligations of, or guaranteed by, the United States or the State of New Jersey or any of its political subdivisions. Pursuant to N.J.A.C. 3:1-4.13, irrevocable stand-by letters of credit issued by the Federal Home Loan Bank of New York are also considered eligible collateral under GUDPA. The Commissioner of Banking and Insurance (Commissioner) has determined that irrevocable stand-by letters of credit and other obligations identified in N.J.S.A. 17:9-41 as eligible collateral should be in a form that is readily marketable and not illiquid in nature. This determination is necessary in order to avoid the possibility that an illiquid and/or not readily marketable obligation will be used as eligible collateral. Were a public depository to utilize such obligations as eligible collateral, its doing so would defeat the intent of GUDPA and lead to the absurd result of permitting public funds on deposit in a public depository to be secured by obligations that cannot be accessed in an expeditious manner, thereby exposing to added jeopardy the very public funds that the collateral was earmarked to secure.

Additionally, it is necessary to exclude illiquid instruments so as not to undermine GUDPA and prevent the fulfillment of its mission of adequately securing deposits of public funds in the event a depository institution becomes insolvent. The Department is therefore

proposing to amend N.J.A.C. 3:1-4.13 by adding new subsection (a) to provide that all instruments of eligible collateral will be in a form that is readily marketable and not illiquid in nature, and to provide that the determination of adequate marketability and liquidity will be made by the Commissioner. That determination will be based upon the existence of a substantial public market for the collateral and a high probability that the collateral can promptly be converted into cash through existing available channels. The existing text of N.J.A.C. 3:1-4.13 will be recodified as new subsection (b).

The Department has determined that the comment period for this proposal shall be 60 days; therefore pursuant to N.J.A.C. 1:30-3.3(a)5, this proposal is excepted from the rulemaking calendar requirement.

Social Impact

The proposed amendment will impact the ability of depository institutions to utilize illiquid types of instruments as eligible collateral for GUDPA deposits. The proposed amendment will increase the sufficiency of eligible collateral pledged by insuring that it is readily marketable and not illiquid in nature, thereby increasing the likelihood that government units will be made whole in the event a depository institution becomes insolvent. The Department anticipates that the proposed amendment will result in increased protections for governmental units and their constituents without being overly burdensome on depository institutions.

Economic Impact

The proposed amendment will likely have a positive economic impact upon public entities that make GUDPA deposits by increasing the likelihood that governmental units will be made whole in the event a public depository institution becomes insolvent. The Department does not anticipate any significant economic impact on depository institutions as a result of the proposed amendment, as the costs involved in posting obligations of sufficient marketability and liquidity are not significantly higher than those that are illiquid in nature and difficult to market.

Federal Standards Statement

The proposed amendment does not contain standards or requirements that exceed standards or requirements imposed by Federal law. The amendment is not subject to any Federal standards or requirements.

Jobs Impact

The Department does not anticipate that any jobs will be lost or generated as a result of the proposed amendment.

Agriculture Industry Impact

The Department does not expect that any agriculture industry impact will result from the proposed amendment.

Regulatory Flexibility Analysis

The Department believes that the proposed amendment will apply to “small businesses” as that term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq. because some public depositories may have fewer than 100 employees and may not be dominant in their field. As discussed in the Economic Impact above, the Department does not believe that the proposed amendment will impose any substantial compliance costs on these entities.

Public depositories that provide eligible collateral for GUPDA deposits in accordance with the proposed amended rule will continue to be required to maintain records of such collateral and provide the reporting required by the Department. The Department does not believe that any additional professional services will be needed by public depositories to comply with the proposed amended rule, as required documentation can continue to be prepared in-house in the regular course of their business.

No distinction is made in compliance requirements for small businesses as the requirements relate to the sufficiency of the eligible collateral for GUDPA deposits. Advancing protections for governmental units is a worthy policy objective irrespective of the size of the depository. Therefore no distinctions are made in the proposed amendment based on the size of the depository. The cost of compliance was discussed above under the section entitled Economic Impact.

Smart Growth Impact

The proposed amendments should have no impact on the achievement of smart growth and implementation of the State Development and Redevelopment Plan.

Full text of this proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

3:1-4.13 Eligible collateral

(a) All eligible collateral authorized by N.J.S.A. 17:9-41 to secure public funds on deposit in a public depository shall be in a form that is readily marketable and shall not be illiquid in nature. The determination of ready marketability and liquidity shall be made by the Commissioner based upon the existence of a substantial public market for the collateral and a high probability that the Commissioner could convert the collateral into cash promptly through existing available channels.

(b) In addition to obligations otherwise authorized in N.J.S.A. 17:9-41, eligible collateral shall also include irrevocable stand-by letters of credit issued by the Federal Home Loan Bank of New York. The Commissioner shall review and approve the form of all such letters of credit proposed by a public depository as eligible collateral under this section. Further, the original letter of credit shall be held by the Commissioner.

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