A public hearing will be held by the Ohio Treasurer of State's Office on Thursday, June 22, 2017 at 10:00 a.m. in the Rhodes State Office Tower located at 30 East Broad Street, Columbus, Ohio 43215.

The purpose of the hearing is to solicit comment on new rules **113-40-01, 113-40-02, 113-40-03, 113-40-04, 113-40-05, and 113-40-06**.

Ohio Pooled Collateral Program Administrative Rules

113-40-01 Definitions

(A) As used in this section:

(1) "Asset quality" means the component within the SCALE model that evaluates risk, controllability, adequacy of loan loss reserves, acceptable earnings, and the effect of off-balance sheet earnings and loss.

(2) "Bank monitoring" means the SCALE model identifying an emerging individual financial concern or a deposit business concern for a financial institution.

(3) "Bank monitoring collateral requirement" means an additional collateral requirement that may be imposed on a financial institution using a reduced collateral floor if the SCALE model identifies an emerging individual financial concern, or a deposit business concern.

(4) "Capital adequacy" means the component within the SCALE model that measures a financial institution to determine if solvency can be maintained due to risks that have been incurred as a course of business.

(5) "Collateral requirement calculation" means the mandatory amount of collateral for a financial institution participating in OPCP, as determined in OPCS based upon the following factors: account balances; Federal Deposit Insurance Corporation coverage as determined pursuant to Rule 113-40-02(A)(2)(a) of the Administrative Code, which may deviate from actual Federal Deposit Insurance Corporation limits; statutory collateral requirement; reduced collateral floor; any bank monitoring collateral requirement(s); any economic monitoring collateral requirement(s); any public unit negotiated collateral requirement(s); and any cushion collateral requirement(s).

(6) "Collateral sufficiency" means the determination made by the treasurer of state on whether a financial institution is adequately collateralized based upon the collateral requirement calculation and the collateral valuation.

(7) "Collateral valuation" means the market value of eligible collateral pledged by a financial institution.

(8) “Cushion collateral requirement” means an additional collateral requirement that may be imposed by the treasurer of state on a financial institution that is not in compliance with collateral sufficiency requirements, file submission requirements, or the operating policies.

(9) “Earnings” means the component within the SCALE model that determines the ability of a financial institution to increase capital through retained earnings, absorb loan losses, support the future growth of assets, and provide a return to investors.

(10) “Economic monitoring” means macroeconomic monitoring and regional economic monitoring under Rule 113-40-05(B) of the Administrative Code.

(11) “Economic monitoring collateral requirement” means an additional collateral requirement that may be imposed on a financial institution using a reduced collateral floor if economic monitoring identifies a potential concerning economic trend.

(12) “Financial institution” means any institution designated as a public depository pursuant to section 135.01 of the Revised Code, and any institution which receives or holds any public deposits as defined in section 135.31 of the Revised Code, or which receives or holds any funds from a public depositor as defined in section 135.182(A)(2) in the Revised Code.

(13) “Influencing variable” means a specific financial indicator used in the SCALE model, which has a benchmark within OPCS that does not need to be met by a financial institution in order to be initially approved for a reduced collateral floor, but a financial institution may be ineligible for a reduced collateral floor if it does not meet a certain number of influencing variables.

(14) “Liquidity” means the component within the SCALE model that measures what a financial institution requires if funding is interrupted and the financial institution must still be able to meet certain obligations, including its ability to repay depositors and other creditors without incurring excessive costs.

(15) “Ohio pooled collateral program” (OPCP) means the program, created by the treasurer of state pursuant to section 135.182(B)(1) of the Revised Code, in which each financial institution that selects the pledging method prescribed in section 135.18(A)(2) of the Revised Code or section 135.37(A)(2) of the Revised Code, shall pledge to the treasurer of state a pool of eligible securities for the benefit of all public depositors at the public depository to secure the repayment of uninsured public deposits at the public depository, and, if applicable, collateral dedicated to a specific public depositor, provided that the total market value of the securities so pledged is at least equal to the amounts required by section 135.182 of the Revised Code.

(16) “Ohio pooled collateral system” (OPCS) means the system created and maintained by the treasurer of state to facilitate financial institution and public unit participation in OPCP via a publicly-available website and private portal access.

(17) “Operating policies” means the set of operational procedures, policies, and requirements for the use of OPCS, to be made available by the treasurer of state. All participation in OPCP and use of OPCS shall be subject to the operating policies, maintained at the sole discretion of the treasurer of state. The operating policies will be available at www.tos.ohio.gov.

(18) “Pooling method” means the method of pledging a security or securities using OPCS, as prescribed in section 135.18(A)(2) or 135.37(A)(2) of the Revised Code.

(19) “Public deposits” means moneys of a public depositor as defined in section 135.182(A)(3) of the Revised Code, but for the purposes of these rules herein, does not include the moneys of metropolitan housing authorities, public or Indian housing agencies, or United States federal agencies.

(20) “Public unit” means the state or a subdivision thereof, as applicable, that deposits public deposits with a financial institution.

(21) “Public unit negotiated collateral requirement” means a collateral requirement negotiated by a public unit with its financial institution, which may differ from the statutory collateral requirement.

(22) “Reduced collateral floor” means a collateral requirement available to eligible financial institutions pursuant to section 135.182(B)(1)(b) of the Revised Code. A financial institution’s reduced collateral floor will be determined in accordance with Rules 113-40-03 through 113-40-06 of the Ohio Administrative Code.

(23) “Required variable” means a specific financial indicator, used in the SCALE model, with a defined benchmark within OPCS that must be met by a financial institution in order to be initially approved for a reduced collateral floor.

(24) “SCALE model” means the model used to determine a financial institution’s reduced collateral floor using the following components, as further defined herein: sensitivity to risk, capital adequacy, asset quality, liquidity, and earnings.

(25) “SCALE component” means an individual component within the SCALE model.

(26) “SCALE component variable” means an influencing or required variable for an individual SCALE component.

(27) “SCALE component score” means the calculation of a financial institution’s individual and peer group based performance against required variables and influencing variables in a single SCALE component score.

(28) “SCALE composite score” means the calculation of a total score for a financial institution using a weighted average of the SCALE components, with weights assigned based on the reflective strength value the SCALE model has determined for each component.

(29) “Sensitivity to risk” means the component within the SCALE model that reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, equity prices, or other factors can adversely affect a financial institution’s earnings or economic capital.

(30) “Specific pledge method” means the method of separately securing uninsured public deposits of each public depositor, as prescribed in section 135.18(A)(1) of the Revised Code.

(31) “Specific pledge account” means an account containing a security or securities pledged for the benefit of one specific public unit by a financial institution participating in the pooling method. A financial institution may be permitted to use a specific pledge account if: the charter for the public unit requires use of the specific pledge method; United States federal law designates the specific pledge method for the public unit; or it is permitted at the discretion of the treasurer of state. Under this method, the financial institution will secure all uninsured deposits at least equal to the requirement for the specific pledge method.

(32) “Statutory collateral requirement” means the amount of collateral required for financial institutions in OPCP pursuant to section 135.182 of the Revised Code.

(B) The treasurer of state will release public records pursuant to public records law.

113-40-02 Requirements for a Financial Institution

(A) All financial institutions participating in OPCP shall:

(1) Transmit files to OPCS, including, but not limited to, up to three files every day the Federal Reserve is open for business;

(2) Pledge sufficient collateral when uninsured public deposits are received;

(a) The treasurer of state will estimate the Federal Deposit Insurance Corporation insurance, which may deviate from actual Federal Deposit Insurance Corporation insurance.

(b) A financial institution must address collateral deficiencies in accordance with the operating policies.

(3) Pledge eligible collateral with a qualified trustee to secure public deposits;

(a) The trustee shall identify and hold collateral pledged to the treasurer of state for the benefit of public units with deposits in the respective financial institution.

(b) The trustee shall hold all collateral pledged to the treasurer of state in one or more identifiable pooled collateral accounts for each financial institution, as specified by the treasurer of state.

(c) A financial institution will pledge collateral to the treasurer of state with a trustee as required, and the trustee will inform the treasurer of state of all new pledges.

(i) The treasurer of state will not accept any statement, communication, or notice from a financial institution as evidence of pledged collateral.

(ii) The treasurer of state will only update OPCS records on receipt of documentation submitted by the trustee.

(4) Submit a collateral release request to the treasurer of state in order to have pledged collateral released by the trustee;

(a) A trustee will only release collateral on the instruction of the treasurer of state, and will not accept requests directly from a financial institution.

(b) Acceptance or denial of a release of collateral request will occur as determined by the treasurer of state.

(5) Not pledge, combine, cross-collateralize, or aggregate pledged collateral in one pool in OPCP for either another pool in OPCP or for the benefit of any other party;

(6) Monitor pledged collateral and submit a collateral release request to the treasurer of state in advance of the maturity date of the pledged collateral;

(7) Be subject to ongoing monitoring for compliance of collateral sufficiency requirements and file submission requirements;

(a) If the treasurer of state determines a financial institution is not in compliance with the operating policies, collateral sufficiency requirements, or file submission requirements, then the treasurer of state may impose a cushion collateral requirement.

(b) Upon entrance into OPCS, the cushion collateral requirement will have a default value of zero.

(8) Report any public unit negotiated collateral requirement at an account level.

113-40-03 Reduced Collateral Floor Application

(A) A financial institution may apply for a reduced collateral floor when they apply for OPCP or following its application to OPCP.

(1) A financial institution must submit an application for a reduced collateral floor to the treasurer of state.

(a) If the treasurer of state approves the application, it will set the reduced collateral floor in OPCS.

(b) If the treasurer of state does not approve the application, it will notify the financial institution.

(2) If the public unit negotiated collateral requirement is higher than the reduced collateral floor, the public unit negotiated collateral requirement will take precedence.

(B) In addition to the criteria listed herein, an eligible financial institution must abide by Rule 113-40-02 of the Administrative Code and this Rule in order to meet the safety and soundness standards of a public depository in accordance with section 135.182(B)(1)(b) of the Revised Code.

(C) Notwithstanding any additional collateral requirements as further detailed herein, a financial institution approved for a reduced collateral floor shall initially be required to secure all uninsured public deposits at least equal to fifty percent.

(D) A financial institution approved for a reduced collateral floor shall not be able to use the reduced collateral floor until it has participated in OPCP for at least thirty calendar days.

113-40-04 Reduced Collateral Floor Criteria

(A) A financial institution participating in OPCP may apply for a reduced collateral floor, which will be evaluated by the treasurer of state, in accordance with the following criteria.

(1) The treasurer of state shall use required variables and influencing variables to determine and maintain the reduced collateral floor for a financial institution. The use of the SCALE model shall be conducted in accordance with the following objectives:

(a) Use data only from publically available sources with no additional reporting requirements from a financial institution;

(b) Evaluate a financial institution both individually, as well as within a defined peer group, against the required and influencing variables as applicable;

(c) Evaluate and take into account trends in the economy in Ohio and nationally;

(d) Evaluate the capacity, nature, and complexity of the financial institution's activities and risk profile, as well as any other pertinent information related to the overall condition of the financial institution; and

(e) Does not imply or construe the treasurer of state as a de facto ratings agency.

(2) A financial institution that applies for a reduced collateral floor will have a SCALE report generated. This report will be available on OPCS.

(3) The SCALE model consists of five components, each containing both required variables and influencing variables further defined in the operating policies, in accordance with the following:

(a) Sensitivity to risk:

(i) Required variables:

(1) De novo status;

(2) Operating assets;

(3) Test for restart stress; and

(4) Federal home loan bank advances to assets ratio.

(ii) Influencing variables:

(1) Publically traded test;

(2) Operating efficiency;

(3) Long-term assets to total assets ratio;

(4) At-risk market assets to lending ratio;

(5) Loans and commitments to assets;

(6) Deposit dollars per lending dollar;

(7) Institutional and miscellaneous lending to total lending ratio;

(8) Reciprocal adjusted brokered deposits to total deposits ratio;

(9) Foreign deposits to total deposits ratio; and

(10) Cost of funds, including the aggregate cost of funds and component costs of funds for selected classes of funding sources.

(b) Capital adequacy:

(i) Required variables:

(1) Common equity tier one ratio;

(2) Tier one leverage ratio;

(3) Tier one to risk weighted assets ratio;

(4) Risk based capital to risk weighted assets ratio;

(4) Tangible common equity ratio;

(5) Supplemental (tier one and tier two) to risk weighted assets ratio; and

(6) Supplemental tier one leverage margin.

(ii) Influencing variable:

(1) Risk-based capital growth rate.

(c) Asset quality:

(i) Required variables:

(1) Risk-adjusted return on economic capital;

(2) Net interest margin annualized;

(3) Texas ratio; and

(4) Credit benchmark, probability of default rating method one and two.

(ii) Influencing variables:

(1) Weighted average maturity;

(2) Economic capital to tier one capital;

(3) Loss given default;

(4) Exposure at default;

(5) Defaults to provisions;

(6) Lending gross default rate;

(7) Troubled lending as percentage of lending;

(8) Loss provisions to adjusted loans; and

(9) One-year loan growth and decline.

(d) Liquidity:

(i) Required variables:

(1) Thirty-day operational liquidity ratio, via cash flows; and

(2) Balance sheet nominal and stress scenario test.

(ii) Influencing variables:

(1) On-hand liquidity to average assets ratio;

(2) Loss absorption capacity margin for uninsured deposit counterparties;

(3) One-year short-term debt service test;

(4) Short-term liabilities to total assets ratio; and

(5) Non-core deposits to total liabilities ratio.

(e) Earnings:

(i) Required variables:

(1) Return on average assets;

(2) Return on adjusted equity; and

(3) Non-interest income to average assets.

(ii) Influencing variables:

(1) Return on tangible assets;

(2) Gross profit rate, year-to-date; and

(3) Return on lending.

(4) A financial institution that applies for a reduced collateral floor will receive both a SCALE component score and a SCALE composite score.

(a) The SCALE component score will be calculated by the financial institution's individual and peer group based performance against the required variables and influencing variables.

(i) The SCALE component score will be calculated based on a one point zero zero to five point zero zero numerical scale.

(ii) A one point zero score indicates strong individual and peer group based performance relative to the financial institution's size, complexity, and risk profile.

(iii) A five point zero score indicates a low level of individual and peer group based performance relative to the financial institution's size, complexity, and risk profile.

(iv) A financial institution cannot score higher than a one point zero, or lower than a five point zero.

(b) The SCALE composite score will be calculated by weighting the SCALE component scores and summing the results. The assigned weights indicate the reflective strength for each SCALE component within the SCALE model.

(i) Sensitivity to risk will have a twenty percent component weight.

(ii) Capital adequacy will have a thirty percent component weight.

(iii) Asset quality will have a twenty percent component weight.

(iv) Liquidity will have a twenty percent component weight.

(v) Earnings will have a ten percent component weight.

(5) The SCALE model will evaluate specific SCALE component variable performance by an individual financial institution against the peer group mean from a representative sample of the peer group. A financial institution seeking and using a reduced collateral floor will be placed into one of six peer groups, based on asset size and other characteristics. The peer groups will not differentiate between commercial and savings banks.

(a) Peer group one will consist of certain United States financial institutions that have been determined by government regulators as global systemically important banking organizations.

(b) Peer group two will consist of financial institutions with assets in excess of ten billion dollars that are not global systemically important banking organizations.

(c) Peer group three will consist of financial institutions with assets in excess of three billion dollars, but less than ten billion dollars, that are not global systemically important banking organizations.

(d) Peer group four will consist of financial institutions with assets in excess of one billion dollars, but less than three billion dollars.

(e) Peer group five will consist of financial institutions with assets in excess of one hundred million dollars, but less than one billion dollars.

(f) Peer group six will consist of financial institutions with assets less than one hundred million dollars.

(6) To be initially approved for a reduced collateral floor, a financial institution must meet all of the following criteria:

(a) Have SCALE component and SCALE composite scores of two point two five or less for the current quarter;

(b) Have SCALE component and SCALE composite scores of two point two five or less for the average of the preceding five quarters;

(c) Meet all of the required variables for the average of the preceding five quarters;

(d) Have no concerning trends related to sensitivity to risk, capital adequacy, asset quality, liquidity, or earnings for a rolling three-year period;

(e) Be in good standing with government regulators with respect to their deposit business;

(f) Not be a de novo bank, as reported by the Federal Deposit Insurance Corporation;

(g) Not receive or have on deposit at any one time public moneys, including public moneys as defined in section 135.31 of the Revised Code, in an aggregate amount in excess of thirty percent of its total assets, pursuant to Revised Code section 135.03; and

(h) Have executed all applicable OPCS and OPCP contracts and documents.

(7) If a financial institution meets the foregoing criteria, but the treasurer of state has identified adverse macroeconomic or regional economic trends or indicators pursuant to the monitoring protocols in Rule 113-40-05(B) of the Administrative Code, then the reduced collateral floor approval may be withheld at the sole discretion of the treasurer of state.

113-40-05 Bank Monitoring and Economic Monitoring

(A) All financial institutions approved for a reduced collateral floor will be subject to ongoing monitoring of various individual financial criteria. If the financial standing of the financial institution changes, and no longer meets the required reduced collateral floor eligibility criteria as defined in Rule 113-40-04 of the Administrative Code, the treasurer of state may impose a bank monitoring collateral requirement. The treasurer of state will use three descriptors within OPCS to identify a financial institution’s reduced collateral monitoring status:

(1) Non-active: The financial institution has not applied, or has not been approved, for a reduced collateral floor.

(2) Active: The financial institution has been approved for a reduced collateral floor.

(3) Bank monitoring: The SCALE model has indicated that the financial institution has an emerging individual financial concern or a deposit business concern.

(a) The treasurer of state will notify a financial institution when its reduced collateral monitoring status changes from active to bank monitoring within OPCS, which will notify the affected public unit(s).

(b) A financial institution subject to a bank monitoring collateral requirement will be subject to an up to fifty-two percent increase in its reduced collateral floor requirement, to a maximum of one hundred and two percent. Any increase will be reflected in the bank monitoring field in OPCS, as determined at the sole discretion of the treasurer of state.

(c) A financial institution subject to an increase in its reduced collateral floor due to bank monitoring status is required to pledge additional collateral on or before the following deadlines:

(i) First collateral call will require a financial institution to secure all uninsured public deposits at least equal to the sum of the reduced collateral floor requirement plus up to ten percent, within ninety calendar days.

(ii) Second collateral call will require a financial institution to secure all uninsured public deposits at least equal to the sum of the reduced collateral floor requirement plus up to twenty-five percent, within sixty calendar days.

(iii) Third collateral call will require a financial institution to secure all uninsured public deposits at least equal to one hundred and two percent, within thirty calendar days.

(d) The treasurer of state may decide to engage a financial institution prior to changing its status from active to bank monitoring in order to identify any extenuating considerations. This decision will be made at the sole discretion of the treasurer of state.

(B) All financial institutions approved for a reduced collateral floor will be subject to economic monitoring protocols to identify potential macroeconomic or regional economic concerns.

(1) The treasurer of state will use two publicly available macroeconomic indicators to identify any potential concerning economic trends:

(a) The smoothed United States recession probability index, in which a negative trend is defined as three consecutive months of smoothed probabilities above eighty percent; and

(b) The ten-year treasury constant maturity minus two-year treasury constant maturity, in which a negative trend is defined as a one-month instance of a negative spread observation.

(2) The treasurer of state will monitor a regional economic indicator, the leading index for Ohio as produced by the Federal Reserve Bank of Philadelphia, in which a negative trend is defined as a negative percentage observation instance occurring in three consecutive months.

(3) If the treasurer of state identifies a potential macroeconomic or regional economic concern, then the treasurer of state may implement an economic monitoring collateral requirement for a specific financial institution, a specific peer group, or an OPCS-wide collateral call, at the sole discretion of the treasurer of state. A financial institution subject to an economic monitoring requirement is required to pledge additional collateral on or before the following deadlines:

(a) First collateral call will require a financial institution to secure all uninsured public deposits at least equal to the sum of the reduced collateral floor requirement plus ten percent, within ninety calendar days.

(b) Second collateral call will require a financial institution to secure all uninsured public deposits at least equal to the sum of the reduced collateral floor requirement plus twenty-five percent, within sixty calendar days.

(c) Third collateral call will require a financial institution to secure all uninsured public deposits at least equal to one hundred two percent, within thirty calendar days.

113-40-06 Collateral Sufficiency

(A) In calculating the collateral percentage required at a bank account level, OPCS will require the greater of the following two calculations:

(1) The public unit negotiated collateral requirement plus the cushion collateral requirement; or

(2) The reduced collateral floor requirement plus any bank monitoring collateral requirement, any economic monitoring requirement, and any cushion collateral requirement.

(B) In calculating collateral sufficiency, the treasurer of state will:

(1) Use existing market pricing available through a reputable source to determine the collateral valuation to calculate the collateral sufficiency.

(a) The treasurer of state will share the source of market pricing.

(b) A financial institution may challenge this collateral valuation, but the treasurer of state shall make the final determination.

(2) Conduct a daily review of collateral sufficiency based upon the collateral requirement calculation and the collateral valuation.

(a) A financial institution may challenge this collateral sufficiency, but the treasurer of state shall make the final determination.

(b) A financial institution will be notified by the treasurer of state of any collateral deficiencies, and will be responsible to address the deficiencies in accordance with the operating policies.