



STATE OF ARKANSAS

Department of Finance and Administration

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To: Bank or Financial Institution

From: Paul S. Louthian, CPA 
Administrator

Subject: Rule 2012-A, *Management of Cash Funds*
Approval of Certain Entities as Custodians

Date: July 13, 2012

Rule 2012-A, *Management of Cash Funds*, was recently promulgated by the State Board of Finance. The Rule becomes effective July 14, 2012. A copy of the Rule accompanies this memo.

The Rule provides requirements for the management of cash funds of state agencies including investment activities and the collateralization of cash funds that are on deposit with banks or financial institutions that exceed coverage by the Federal Deposit Insurance Corporation (FDIC).

Current Federal Deposit Insurance Corporation (FDIC) coverage provides unlimited deposit insurance on non-interest-bearing transactional accounts. The unlimited coverage will expire January 1, 2013. In order to meet this deadline, all state agencies with cash funds subject to the Rule will need to comply with requirements of the Rule by October 31, 2012.

Section E, paragraph 4, of the Rule addresses custodial services or pledged collateral. Certain entities are allowed by the Rule to be used as custodians. Other entities will require approval by the State Board of Finance in order to be used as a custodian.

The following entities are allowed by the Rule to provide custodial services without further approval of the State Board of Finance:

1. Any Federal Reserve Bank
2. Any Federal Home Loan Bank

3. A banker's bank
4. A trust department, or similar safekeeping function, of a commercial bank or trust company that is:
 - a. Primarily located within the State of Arkansas, and
 - b. Unaffiliated with the bank or financial institution holding the collateralized cash fund deposits.

“Unaffiliated” is defined in paragraph 4.d. of Section E of the Rule. The Rule specifies that ownership of up to 5% of the outstanding voting securities custodian by the bank or financial institution, or of the bank or financial institution by the custodian, is considered a *de minimus* interest and the two entities could be considered “unaffiliated”.

The following entities require specific approval of the State Board of Finance:

1. The trust department, or similar safekeeping function, of a commercial bank or trust company primarily located outside the State of Arkansas, and
2. A securities broker or dealer.

To request permission to use one of the above entities as custodian, the following procedures shall be followed:

1. The requesting party shall submit a written request to the Director of the Department of Finance and Administration. The written request shall consist of:
 - a. A completed Request for Approval form.
 - b. A cover letter that provides a narrative supporting the request and does not exceed three pages.
 - c. Any other documents that support the request.
2. To assist state agencies with initial compliance with the Rule, the written request should be submitted by September 15, 2012.
3. The Director of the Department of Finance and Administration and the State Banking Commissioner shall initiate a review the written request to determine if the proposed custodian has the financial stability, experience, technical skill, and staffing levels necessary to perform custodial services.
4. A committee shall be appointed to conduct the review. The committee shall consist of three members being one representative of the Department of Finance and Administration, State Banking Department, and Office of State Treasurer. The committee shall review the request and submit its findings to the Director of the Department of Finance and Administration and the State Banking Commissioner.
5. Additional information may be requested of the requesting party to facilitate the review.

6. A recommendation regarding the request shall be made to the State Board of Finance upon completion of the review.
 - a. The recommendation will be submitted to the members of the State Board of Finance for their consideration. If no objection is received from any Board member within 10 business days after the submission of the recommendation, the recommendation shall be considered adopted.
 - b. If any Board member objects to the recommendation, the recommendations shall be considered and acted on at a meeting of the State Board of Finance.
 - c. A requesting party may appeal a denial of a request for approval according to the provisions of the Administrative Procedures Act.