



State Treasurer of Ohio  
Ohio Pooled Collateral System (OPCS)

April 13, 2017

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OPCS Background

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**OPCS**

FOR DISCUSSION  
**DRAFT**  
PURPOSES ONLY

- The Ohio Pooled Collateral System (OPCS) allows for participating Financial Institutions (FI) to pool collateral for Ohio Public Unit's (PU) deposits.
- The Treasurer of State (TOS) is the sole administrator and monitor of the program.
- FI's will chose to 1) participate in the pooling method (OPCS) collateralizing at 102% or a rate set by the Treasurer in rule or 2) not participate in OPCS and collateralize all public entities with specific pledge method at 105%.



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**OPCS Stakeholders**

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- TOS: Treasurer of State – charged with the creation and implementation of the Ohio Pooled Collateral System
- Financial Institutions (FI): Banks that are qualified public depositories in Ohio
- Build Banks: Six banks that have volunteered to assist TOS with the creation of the system
- Public Units (PU): Local Governments in Ohio (i.e. Cities, Townships, Counties, Villages, Special Districts)
- Trustees: entities approved by the Ohio Department of Commerce as Collateral Trustees or entities approved as Collateral Trustees in the Ohio Revised Code

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**Monitoring Responsibility**

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- **Specific Pledge Method**  
Responsibility for monitoring the FI's compliance falls solely on the public entity who is required to maintain a record of all securities pledged at all times.
- **Pooling Method**  
TOS is responsible for monitoring the FI's collateral levels and compliance. The FI will be required to electronically report to the OPCS. The FI may choose any eligible and approved collateral trustee and pledge a single pool of collateral through OPCS for all of the FI's uninsured Ohio public entity deposits.

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**Benefits of OPCS**

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- Centralized collateral monitoring will save time and resources for local governments by shifting the administrative burden for managing pledged collateral to the Treasurer of State.
- Provides administrative benefits for financial institutions by streamlining the processing and management of pledged collateral.
- Guards against fraud since the TOS will be able to see all pledged collateral compared to the total amount of public deposits at a financial institution.
- OPCS does not impact a local governments ability to select which eligible institution will hold its deposits.

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**Public Unit Responsibilities**

Responsibilities for Public Units with Deposits in an OPCS Participating FI:

- The Treasurer of State will provide market pricing of all collateral and publish the reports on the OPCS portal.
  - Public Units will be responsible for reviewing and monitoring the reports posted, verifying the accuracy of reports of their itemized deposits, and reporting any discrepancies to their financial institution.
- The Treasurer of State will provide OPCS access to the public units.
- Public units shall periodically certify account details, including deposit balances, and contact details are correct, in accordance with the schedule set by the Treasurer of State.
- Public Units may negotiate a public unit negotiated collateral requirement for individual accounts with their financial institution, which may be higher than the statutory collateral requirement or the reduced collateral floor as applicable.

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Overview

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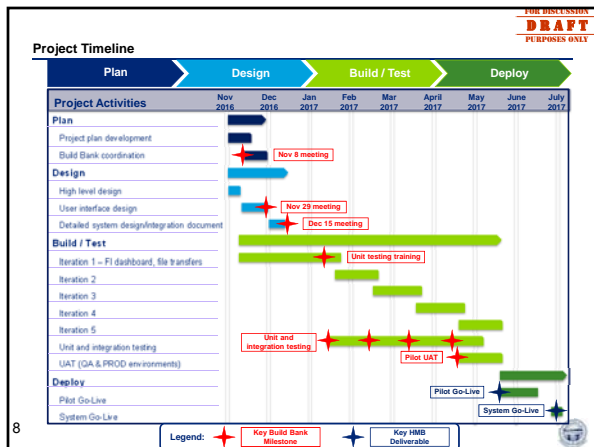
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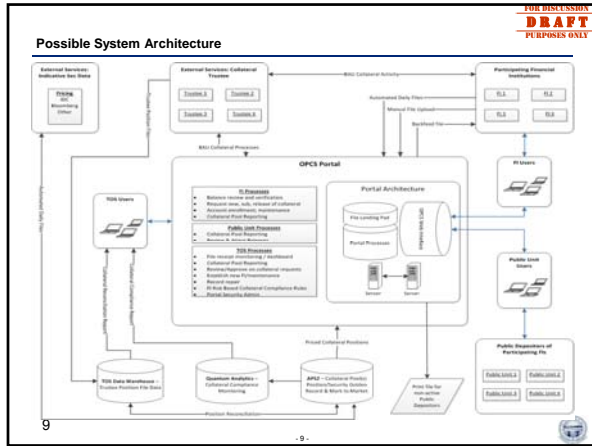
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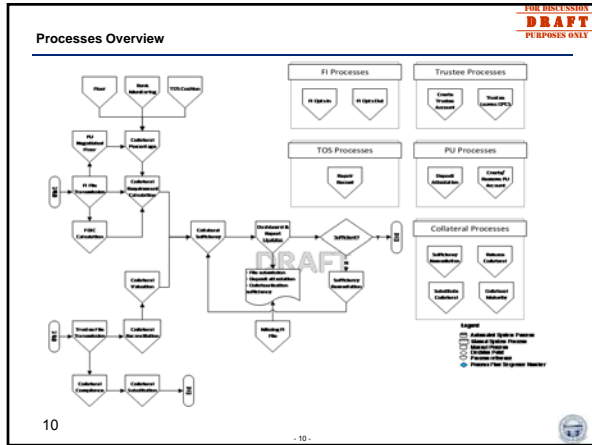
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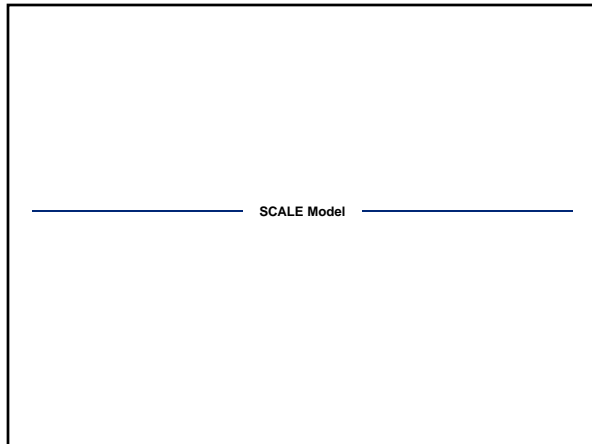
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**Model Objectives**

The Treasurer's Office is using the following objectives when drafting the Model:

- Be stringent, but fair
- Be transparent, objective, and externally reproducible – be predictable
- Only use data for evaluation from externally and publically available sources, no additional data requested from FIs
- Evaluate a FI's micro-economic condition, as well as its relative position to Ohio, regional, and national peer groups
- Evaluate and take into account macro-economic issues impacting the banking sector
- Recognize and risk account when external market data elements are unavailable for a FI

The model does not imply, create, or construe the Treasurer's Office as a de facto ratings agency



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**Components**

**SCALE Components**

**Sensitivity to Risk** is the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a bank's earnings or economic capital.

**Capital Adequacy** is a measurement of a bank to determine if solvency can be maintained due to risks that have been incurred as a course of business.

**Asset Quality** evaluates risk, controllability, adequacy of loan loss reserves, and acceptable earnings; and the effect of off-balance sheet earnings and loss.

**Liquidity** is what a bank requires if funding is interrupted and the bank must still be able to meet certain obligations, i.e. the bank's ability to repay depositors and other creditors without incurring excessive costs.

**Earnings** determine the ability of a bank to increase capital (through retained earnings), absorb loan losses, support the future growth of assets, and provide a return to investors.



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**Component and Composite Score System**

A FI will receive a score for each of the five SCALE Components which will in turn be used to determine the SCALE Composite score.

**SCALE Component Ratings**

The SCALE Component scores are assigned based on a 1 to 5 numerical scale:

- A "1" score indicates strong individual and peer based performance relative to the institution's size, complexity, and risk profile.
- A "5" score indicates a low level of individual and peer based performance relative to the institution's size, complexity, and risk profile.

**SCALE Composite Rating**

The SCALE Composite rating generally bears a close relationship to the SCALE Component ratings but is not derived by an average of the SCALE Component ratings:

- The Composite score is based on the weight the SCALE model assigns to each Component.



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**Component Score Concepts**

- Unlike the CAMELS rating system in place with Federal regulators, each SCALE Component score is solely determined mathematically. This ensures objective and reproducible analysis is applied consistently across all participating FIs.
- A FI's Component score is determined through evaluation of both required variables ("Required Variable") and influencing variables ("Influencing Variable").
- A Component score is calculated by a FI's individual and peer group based performance against Required Variables and Influencing Variables.
- A FI cannot score higher than 1.00 or lower than 5.00.




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**Peer Grouping**

SCALE benchmarks FIs to their peer groups to evaluate Component variable relative performance against an individual FI's peer group mean. The SCALE peer grouping ("Peer Group") is based on a modified version of the federal uniform bank performance reporting (UBPR) peering rules.

Rule Based Collateral participating FIs are grouped into one of six OPCS Peer Groups based on the FI's asset size and other characteristics. None of the six Peer Groups differentiates between commercial and savings banks types. Peer Groups are still under review and are subject to change.

Peer Group #	Asset Class	GSIB*	Approximate # in Peer Group Sample**	Approximate # in Ohio
<b>Group 1</b>	> \$10 billion	Yes	8	4
<b>Group 2</b>	> \$10 billion	No	100	14
<b>Group 3</b>	> \$3 billion, < \$10 billion	No	185	14
<b>Group 4</b>	> \$1 billion, < \$3 billion	No	440	13
<b>Group 5</b>	> \$100 million, < \$1 billion	No	390	125
<b>Group 6</b>	< \$100 million	No	390	60

\* Global systemically important banking organizations (GSIB) have been designated as such. Currently there are eight U.S. firms identified as GSIBs.  
 \*\* All Ohio FIs in each peer group are included in the Peer Group Sample.




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**Component Scoring - Review**

It is anticipated, but not finalized, the following calculation methodology will be used to calculate Component scores.

Each variable will be calculated for every FI applying for a Reduced Collateral Floor. The result will first be compared to the benchmark determined for the variable and then compared to Peer Group FIs to calculate its Standard Deviation (SD).

		Initial Component Score:	1.0
Step 1. Bench Mark Comparison	A. Required Variable	Pass:	+0
		Fail:	Component Score = 5.0
Step 2. Standard Deviation (SD) from Peer Group	B. Influencing Variable	Meets:	+0
		Does Not Meet:	+0.25
		SD between 1.0 and 2.0:	+0.25
		SD > 2.0:	+0.50
		<b>Final Component Score :</b>	<b>Add results of each calculated variable to initial component score</b>




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**Reduced Collateral Determination**

- FIs who apply for and are approved for a reduced collateral floor by meeting the application requirements will be granted an initial State Collateral Floor of 50%.
- FIs who apply for and are not approved for a reduced collateral floor will remain on the State Collateral Floor of 102%.
- FIs who do not apply for a reduced collateral floor will remain on the State Collateral Floor of 102%.
- Simplified component scoring methodology.
- The Treasurer's Office is considering including a secondary evaluation organization as an additional data point to complement SCALE.



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**Reduced Collateral Floor Application Requirements - Review**

- A SCALE Composite and Component score of 2.25 or less for the current quarter;
- A SCALE Composite and Component average score of 2.25 for the past five quarters;
- Have no concerning sensitivity, capital, asset, liquidity, or earnings trends for a rolling 3 year period;
- Be in good standing with government regulators with respect to their deposit business;
- Not be a de novo bank as reported by the FDIC;
- Have no more than 30% of total assets comprised of Ohio public deposits; and
- The Treasurer's Office has not detected any adverse macro-economic or bank sector indicators or trends.

FIs that fail to meet these requirements will not be approved for a reduced collateral floor and their collateral requirement will remain at the statutory level of 102%



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**Macro-Economic Monitoring**

The Treasurer's Office will be utilizing macro-economic monitoring protocols to identify potentially emerging economic concerns that might require an overall OPCS program level collateral call for participating reduced collateral FIs.

**Macro-economic Indicators**

- **Smoothed U.S. Recession Probability Index:**
  - Government generated leading indicator that tracks four monthly variables;
    1. Nonfarm payroll employment,
    2. Index of industrial production,
    3. Real personal income excluding transfer payments, and
    4. Real manufacturing and trade sales.
  - Negative trend is defined as three consecutive months of smoothed probabilities above 80%.
- **10-Year Treasury Constant Maturity Minus 2-Year Treasury Constant Maturity:**
  - Market generated statistic that evaluates the spread between interest rates on 10-year U.S. Treasuries and 2-Year U.S. Treasuries.
  - Negative trend is defined as a one month instance of a negative spread observation.
- Both of these variables are produced and are publically available via the St. Louis Federal Reserve's website with Federal Reserve Economic Data ("FRED"); <https://fred.stlouisfed.org/>



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### Regional Economic Monitoring

The Treasurer's Office will be utilizing banking sector monitoring protocols to identify potentially emerging economic concerns that might require an overall OPCS program level collateral call for participating reduced collateral FIs.

#### Regional Economic Indicators

- The Treasurer of State will monitor an Ohio-specific leading economic indicator, the leading index for Ohio as produced by the Federal Bank of Philadelphia, in which a negative trend is defined a negative percentage observation instance occurring in three consecutive months.




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### Bank and Economic Monitoring Action Steps

If a negative FI or macro-economic trend is determined, the Treasurer's Office may, at their sole discretion, implement a specific FI, Peer Group or OPCS wide collateral call via the Bank Monitoring and/or Economic Monitoring escalation process.

#### Active

- FIs statutory collateral requirement
- Determined by OPCS rules and implemented upon approval

#### Action 1

- Additional 0-10% to statutory collateral requirement (not to exceed 102%)
- ≤90 days to meet increased collateral requirement

#### Action 2

- Additional 10-25% to statutory collateral requirement (not to exceed 102%)
- ≤60 days to meet increased collateral requirement

#### Action 3

- Statutory collateral requirement increased to 102%
- ≤30 days to meet increased collateral requirement




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### SCALE – Component Values

Component	Variable	Variable Type	Variable Lower Limit	Variable Upper Limit	SD Impact
Solvency	Debt Ratio	Ratio	50%	50%	N/A
	Operating Assets	Required	70.00%	80.00%	Positive & Negative
	Debt for Related Assets	Required	80.00%	80.00%	N/A
	FICA Advances-to-Assets	Required	0.00%	15.00%	Positive
	Publicly Traded Debt	Information	Yes	Yes	N/A
	Operating Efficiency	Information	N/A	85.00%	Positive
	Bank Asset Assets/Total Assets	Information	0.00%	90.00%	Positive
	De-Risk Market Assets to Underlie Ratio	Information	0.00%	0.00%	Positive
	Ratio and Commitment Exposure Leverage	Information	0.00%	100.00%	Positive
	Lending Support from Deposits	Information	0.00%	N/A	Negative
	Provisional & Misc Lending to Total Lending	Information	0.00%	10.00%	Positive
	Provisional Adjusted Deposits to Total Deposits	Information	0.00%	10.00%	Positive
	Foreign Deposits to Total Deposits	Information	0.00%	10.00%	Positive
Ratio of Funds Test	Information	N/A	N/A	±1.00 SD or less than Peer Group	

Component	Variable	Variable Type	Variable Lower Limit	Variable Upper Limit	SD Impact
Capital Adequacy	Common Equity Tier 1 Ratio (CET1)	Required	8.00%	N/A	Negative
	Tier 1 Leverage Ratio	Required	5.00%	N/A	Negative
	Tier 1 to Risk-Weighted Assets Ratio	Required	8.00%	N/A	Negative
	Risk Based Capital to Risk-Weighted Assets Ratio	Required	10.00%	N/A	Negative
	Weighted Common Equity Ratio	Required	8.00%	N/A	Negative
	Supplemental T1-to-Risk Ratio	Required	8.00%	N/A	Negative
	Supplemental T1 Leverage Margin	Required	2.00%	N/A	Negative
Risk Based Capital Growth Rate	Information	0.00%	N/A	Negative	




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**SCALE – Component Values**

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Component	Variable	Variable Type	Variable Lower Limit	Variable Upper Limit	SD Impact
Asset Quality	Non-Performing Assets as % of Total Assets	Required	0.00%	N/A	Positive
	Non-Performing Assets (Non-Performing Assets)	Required	2.00%	N/A	Positive
	Non-Performing Assets	Required	0.00%	0.00%	Positive
	Bank's Credit Benchmark – PD Rating Method 1 & 2	Required	0.00%	N/A	Positive
	Capital Asset Ratio	Required	11.00%	11.00%	N/A
	Capital Asset Ratio (if Risk-Adjusted than Tier 1 Capital)	Required	8.00%	8.00%	Positive
	Return on Assets (ROA)	Required	0.00%	0.00%	Positive
	Return on Assets (if Risk-Adjusted)	Required	0.00%	0.00%	Positive
	Asset Liquidity	Required	N/A	N/A	0.00 SD at least
	Provision Ratio as % of Total Assets	Required	0.00%	0.00%	Positive
	Non-Performing Assets as % of Total Assets	Required	N/A	0.00%	Positive
	Return on Assets (ROA)	Required	0.00%	N/A	Negative
	Return on Assets (if Risk-Adjusted)	Required	0.00%	N/A	Negative
	Return on Assets (ROA)	Required	0.00%	N/A	Positive
Liquidity	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
Liquidity	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative
	Ratio of Liquid Assets to Total Assets	Required	0.00%	N/A	Negative



# Questions

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