FEATURE ARTICLE

The California Bankers Association Proposes To Rewrite California Banking Law: The Ultimate Blank Check*

*by Gail K. Hillebrand***

INTRODUCTION

The California Bankers Association is currently sponsoring Assembly Bill 2521 (Johnston, Vuich). This bill, which is a two-year bill pending in the Assembly Finance and Insurance Committee, proposes to rewrite the entire California Financial Code division dealing with banks. The bill exceeds three hundred pages in printed form. It would repeal hundreds of current sections of Division One of the Financial Code and add 494 new sections of code. It proposes hundreds if not thousands of changes in the language of current law. The Superintendent of Banking has described the bill as one which "tilts the balance" in favor of the banking industry. Testifying before a joint hearing of the Assembly Finance and Insurance Committee and the Senate Banking Committee, the Superintendent also stated that there is no urgent need to rewrite the banking law. He said, "The banking law does work...we should be very careful about breaking it."[1]

As created in the Financial Code,[2] the State Department of Banking licenses and regulates state-chartered banks, offices of foreign (other nation) banks doing business in California, and trust companies. Under the current banking law, state-chartered and foreign banks must secure the approval of the Superintendent of Banking to merge with another bank,[3] sell the bank or a business unit of the bank,[4] acquire another bank,[5] open or close a branch office,[6] engage in transactions with members of the board of directors or officers,[7] or engage in certain other activities. Among the Superintendent's responsibilities are seeking a conservatorship over banking institutions which are incompetent or insolvent, and liquidating insolvent banking institutions.[8] In 1987 alone, five state-chartered banks failed.[9]

Some of the largest banks operating in California have federal charters and therefore are regulated principally by the Office of the Comptroller of the Currency of the U.S. Treasury, rather than by the State Department of Banking.[10] The banks regulated by the Department, however, constitute a significant portion of the California market. According to the most recent completed annual report of the State Department of Banking, there are 279 state-chartered banks with 1,683 branches throughout California.[11] These banks have assets of $91.2 billion.[12] The number of state-chartered banks increased 66% in the decade from 1978 to 1987.[13] The fourth largest bank in California, First Interstate, is state-chartered.

Foreign banks regulated by the Department of Banking also are a significant presence in California. Eleven of California's top 25 banks are subsidiaries of foreign banks. In addition, offices of foreign banks which do not have separately chartered California subsidiaries have assets of $68.3 million in California.[14]

Banking regulation addresses the entry into and conduct of the banking business for the purpose of protecting the public.[15] Consumers are protected through the Department's enforcement of specific laws governing bank conduct, and are protected from bank insolvency through the significant but indirect means of enforcing laws designed to prevent activities that might weaken a bank's financial condition, such as failure to diversify investments, bad management, or self-dealing transactions which might drain the bank of necessary capital or wrongly transfer its assets. With these purposes in mind, the current banking law absolutely prohibits certain conduct, and allows other conduct only with the permission of the Superintendent of Banking. The California Bankers Association's proposal would both eliminate certain prohibitions and make it easier to secure permission to engage in other activities.

It is impossible to predict all the effects of the bankers' extensive proposal to rewrite the banking law. Problems may be created by repealing existing sections and rewriting them in new language, including confusion about the application of interpretations of current sections to new and rewritten sections. There are also numerous specific ways in which the changes proposed in this bill would directly harm consumers. First, the bill would hurt consumers by weakening the regulatory powers of the Superintendent of Banking. Second, the bill would reduce specific existing consumer rights, including the right to prevent a bank from seizing customer funds in low-balance checking accounts to set off against a debt to the bank, the right to seek damages against a bank which has violated a consumer protection statute, the right to withdraw funds from a certificate of deposit if the deposit is sold to another bank, and other rights. Finally, the bill fails to address serious problems which consumers have experienced with banks. These problems raise a fundamental concern about the appropriateness of the banking industry proposing to rewrite the law which governs its activities.

THE BILL WOULD HARM CONSUMERS BY WEAKENING BANK REGULATION

The changes proposed by AB 2521 would weaken bank regulation in a number of important ways. First, the bill would direct the Superintendent to act to "facilitate" the banking business. It would create ambiguity in the statutory standards for Banking Department approval of sales, mergers, and similar

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**Editor's Note: The Center for Public Interest Law invited the California Bankers Association to participate in this article, which we intended to publish in a point-counterpoint format. We sought CBA's purposes behind AB 2521 and its responses to Consumers Union's concerns about the bill. CBA declined to participate.*

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transactions. It would permit anticompetitive bank sales and mergers even when the harm to competition is not outweighed by any expected benefit of the sale or merger. It would establish strict timelines for the Superintendent of Banking to act on applications by banks for regulatory approval, and would require that many types of applications are automatically approved if the timelines are not met. It would also limit the power of the Superintendent to refer suspected violations of civil laws to city attorneys, district attorneys, and the Attorney General for civil prosecution. Finally, the bill would create new discretion in the Superintendent of Banking to reduce the degree of regulation of the banking industry. It would allow the Superintendent to exempt banks from statutory and regulatory requirements, to decide that whole classes of activity need not be regulated at all, or to waive any regulation of the Department of Banking.

AB 2521 Directs The Superintendent to "Facilitate" the Business of Banking

The bill directs the Superintendent of Banking to exercise his or her powers "in a manner that facilitates the conduct of the banking and trust businesses within this state and promotes the financial safety and soundness of these businesses...."[16] This part of the bill reveals, perhaps unintentionally, the underlying philosophy of the Bankers Association's proposal: that banking regulation should serve the banking industry.

AB 2521 May Permit Transactions Which Adversely Affect Competition

Presently, a bank may not merge with another bank, buy the assets of another bank, or acquire control of another bank without approval of the Superintendent of Banking.[17] Current law permits approval of such transactions only if any anticompetitive effects of the transactions are clearly outweighed by the probable improvement in public convenience, and the transaction will not "result in a monopoly."[18] AB 2521 keeps the requirement that mergers and sales not result in a monopoly, but eliminates the Superintendent's required examination of other effects on competition.[19]

Retention of the "no-monopoly" standard is not enough to protect the competitive environment. An acquisition of control can have an anticompetitive effect without resulting in a monopoly. For example, according to statistics for 1988 reported in American Banker Statistical Special *Top Numbers 1989*, the three banks in California with the largest market share of deposits had 72.8% of the total amount of deposits held by the top fourteen commercial bank deposit takers. The top four banks had 81.4% of these deposits. The total deposits held by the single largest deposit-taking commercial bank was 34 times greater than the deposits held by the tenth largest deposit taker, and 62 times greater than the deposits held by the fourteenth largest deposit taker. These statistics demonstrate a continuing need to fully examine the effects on competition of proposed bank sales and mergers.

Californians need a competitive banking system. Economists at the Federal Reserve have reported that banking in California "is characterized by a higher degree of concentration than markets in other major banking states."[20] Banks in California have historically paid lower interest on deposits and charged higher interest rates on consumer loans than banks in other states.[21] The California Bankers Association has responded to expressions of concern about the deletion of the effect on competition test by pointing out that banks and trust companies remain subject to the antitrust laws. However, an antitrust suit to enjoin or undo a transaction is an inadequate substitute for careful review by the regulator of the effect of the transaction on competition before the transaction is first approved.[22]

The Bill Would Make Regulatory Standards Ambiguous

Current law allows the Superintendent to approve applications for permission to engage in various activities such as sales of a bank, bank mergers, and acquisition of control of a bank *only* if each criterion set forth in the relevant statutory section is satisfied.[23] These conditions compel disapproval of a merger if the transaction would result in a monopoly; the financial condition of an entity acquiring a bank or trust company would be detrimental to the financial condition of the bank or trust company; the competence, experience, and integrity of the acquiring person shows that it would not be in the best interest of the depositors, creditors, shareholders, or the public to permit that person to control the bank; the proposed acquisition is unfair, unjust, or inequitable to the depositors, creditors, or shareholders of the acquired bank or the acquiring entity; or the applicant for approval fails or refuses to furnish all the information required by the Superintendent of Banking.[24]

Under AB 2521, the Superintendent of Banking could approve a sale, merger, or acquisition of control of a bank or trust company even if the transaction fails one or more of these tests.[25] The bill identifies "decisional criteria" which "must be considered", but does not require that an application for sale or merger of a bank must be denied if any statutory criterion is not met.[26]

Many commentators believe that the ongoing crisis in the savings and loan industry was caused in part by inadequate regulatory oversight. In light of the serious dangers of lax regulation, it is inappropriate to restructure the Financial Code so that the Superintendent of Banking need only "consider" various factors, and to allow the Superintendent to approve a sale, merger, acquisition of control, or other bank activity even if the statutory standards are not satisfied.

AB 2521 Requires Automatic Approval of Certain Applications If the Superintendent Does Not Act Within Strict Timeframes

The bill proposes a regulatory approval process using the so-called "deemed approval" mechanism.[27] This means that for many kinds of decisions, the Superintendent's failure to act within strict timelines on an application by a bank or trust company for approval of some activity would result in automatic approval of that activity. Certain types of applications—such as those for approval of voluntary liquidation of a bank or trust company, purchases of a bank, mergers, or acquisitions of control—would not be deemed approved, but the bill would nonetheless set a deadline for decisions on each of these matters.[28]

The "deemed approval" mechanism may deprive the State Department of Banking of the time it needs to fully evaluate applications by banks and trust companies. This weakness of a "deemed approval" regulatory method is compounded by the bill's very short time limits for actions by the Superintendent. The basic time period is only 91 days.[29] The period for approval may be extended beyond 91 days only in "extraordinary circumstances."[30] These short timeframes and automatic approval provisions may make it very difficult for the Superintendent to fully evaluate the effect on the public and on bank safety and soundness

of proposed bank activities, while at the same time fulfilling the Department's ongoing function of supervising existing banks. As the Department of Banking recently stated in a letter on the bill:

> The primary responsibility of the Superintendent is to ensure safety and soundness of banks. Accordingly, the Department should be able to give priority to functions that directly support safety and soundness, such as making examinations, taking enforcement actions, and closing banks. However, establishing rigid timeframes for processing applications would make the Department 'driven' by applications, and allocation of the Department's resources would be dictated by application filings, which are beyond the power of the Department to either predict or control. Such a result would be contrary to the interest of safety and soundness.[31]

AB 2521 Restricts the Superintendent's Ability to Refer Violations of Law for Civil Prosecution

AB 2521 narrowly limits the authority of the Superintendent to refer evidence of an apparent violation of law. The bill would permit the Superintendent to refer evidence to state, local or federal agencies which may indicate a violation of law only if the conduct "is punishable as a crime."[32] However, many important consumer protection statutes are enforced as a matter of civil law by the Attorney General, district attorneys, city attorneys, and others. The Superintendent should be free to refer evidence of potential violations of both civil and criminal laws to all appropriate state and federal enforcement agencies. If this topic is to be directly addressed in a rewrite, the proposed new section should require or at least presume the appropriateness of referral by the regulator of all civil and criminal violations to law enforcement authorities.

The Bill Proposes an Inappropriate Level of Regulatory Discretion

At the same time that it increases administrative discretion with respect to regulatory approvals, AB 2521 also would provide the Superintendent with a new, more liberal standard to allow the Superintendent to exempt banks from regulations and orders.[33] For example, proposed section 204(c) would permit the Superintendent to waive any existing regulation or order whenever he or she deems it to be either in the public interest or "necessary or appropriate...." Current law limits waiver to instances where the Superintendent makes a finding that compliance is "not necessary in the public interest."[34]

The ongoing crisis in the savings and loan industry has all too clearly shown the serious results of overly lenient regulation, particularly at a time when institutions are receiving new powers. In a recent special report by the *San Francisco Chronicle*, the owner of one thrift association was quoted as describing this period in the savings and loan association industry's history as "a crook's paradise."[35]

The purpose of statutory restrictions and statutory standards is to ensure that regulators do in fact apply adequate standards. Regulatory statutes are meaningless if they set forth standards on the one hand and then give the regulator broad power to exempt the regulated from those standards on the other hand. Vague standards for regulatory action make it very difficult to challenge a decision of a regulator which allows too much freedom of action to a regulated entity. A standardless delegation of legislative authority to a regulator also compels the regulator to spend more of his or her time justifying decisions, since he or she cannot merely point to a prohibition or a well-defined standard in current law to justify a denial of a requested exemption. Finally, vague standards ultimately consign the adequacy of regulation to the whim of the regulator.

The Bill Would Repeal Existing Conflict of Interest Provisions

AB 2521 would repeal Financial Code section 234, which sets forth a list of transactions with banks that are forbidden to the Superintendent and to Department of Banking employees. The bill would replace this clear list of prohibited conduct in current law with a direction to the Superintendent to promulgate a code of ethics for Department personnel.[36] Although there is nothing wrong with a code of ethics, a statute which directs preparation of such a code should require it to cover at least those activities now prohibited by the Financial Code.

AB 2521 Would Allow Certain Self-Dealing Transactions Without Regulatory Approval

Presently, a bank may not engage in transactions with its officers, members of its board of directors, or with owning entities without the permission of the Superintendent of Banking.[37] AB 2521 would weaken this provision by permitting such self-dealing transactions without any notice to the regulator or any regulatory approval so long as the amount of the transaction is less than $500,000 or 1% of the bank's gross capital.[38]

THE BANKERS' PROPOSAL REDUCES CONSUMER RIGHTS

AB 2521 proposes changes in the law which would hurt consumers. It would exempt nationally-chartered banks from a variety of consumer protection statutes; immunize banks for a broad variety of violations of consumer, civil rights, and other statutes; fail to prevent harmful branch closings; allow banks to prevent public access to information filed with the State Department of Banking; require consumers to pay a bank's attorneys' fees; and eliminate other consumer rights.

The Bill May Exempt National Banks from Many Consumer Protection Provisions of the Banking Code

The bill may exempt national banks from certain consumer protection provisions now applicable to them, as a result of the proposed redefinition of the term "bank" in AB 2521. The bill would define "bank" as those entities licensed under the state Banking Law to receive deposits.[39] This does not include federally-chartered banks. Thus, where the term "bank" is used in AB 2521, unless otherwise stated in the chapter, it refers only to state-chartered banks, unlike the present code. By reenacting existing consumer protection provisions using the term "bank", while changing the definition of that term, AB 2521 may have the effect of exempting national banks from those provisions. The affected provisions cover deposit account disclosure requirements, consumer rights to notice and other protections in a banker's set-off of a consumer deposit against a debt owed to the bank, and other provisions.[40]

The bill would confer on nationally-chartered banks all the rights, powers, and immunities of state-chartered banks.[41] At the same time, AB 2521 would reduce the powers of the Superintendent of Banking over national banks. At present, the Superintendent requires reports from nationally-chartered banks, but AB 2521 would eliminate that power by limiting its definition of "bank" to cover only state-chartered and foreign banks.[42]

There is no reason why the Superintendent should not have power over national banks conducting business in California, at least to secure information and to enforce state consumer protection statutes.

The Bill Creates Broad New Immunities from Suit for Banks and Trust Companies

AB 2521 would immunize banks and trust companies from liability for a broad variety of violations of law if they simply correct the violation after the fact.[43] No such broad immunity provision exists in the current Banking Law.[44] An immunity from liability would seriously undermine the incentives to comply with various consumer protection and penalty statutes. Consumer protection statutes which authorize the imposition of civil damages or penalties encourage banks to design their forms and procedures to comply with the law. The proposed immunity provisions turn the principle of consumer protection on its head. AB 2521 would allow banks one "free bite"; that is, the ability to escape liability for many types of violations if the bank merely corrects a violation after—and if—it is discovered by consumers or the regulator.

Proposed section 447(a) of the bill provides that illegal activities of a bank or trust company are "deemed" to be in compliance with the law so long as the violation is not intentional, results from bona fide error in spite of reasonable procedures to avoid the error, and is corrected within sixty days of discovery. The section would prevent *all* civil liability arising under *any* state law for such corrected errors. That immunity arguably could apply even to violations of laws other than the banking law, such as California's civil rights statute[45] and its laws against false advertising[46] and unfair and deceptive business practices.[47] No other state statute offers such broad immunity to any industry.[48]

This immunity from all civil liability could be interpreted to immunize banks even from suits to declare their conduct illegal and enjoin it in the future. Further, the section does not clearly require that correction be made for every person or account affected by the violation in addition to the person who complains. Thus, a bank or trust company might try to secure a defense to civil litigation under this section by correcting its error with respect to the consumer who complains, without investigating whether the illegal practice has affected other customers and without correcting the violation affecting those persons.

Proposed section 447(b) of AB 2521 would immunize banks from civil liability and civil penalties under the Banking Law for any act done or omitted "in good faith conformity" with any rule, regulation, written interpretation, order, or approval of the Superintendent of Banking. Any bank or trust company could attempt to secure this protection simply by obtaining an opinion from its lawyer that a contemplated act is "in conformity" with current rules, regulations, interpretations, orders, or approvals of the Superintendent. As drafted, this section could arguably protect a bank when it engages in voluntary conduct not clearly forbidden by a specific regulation, interpretation, order or approval of the Department of Banking, even if it is not required by any law or order to engage in that conduct.

Proposed section 447(c) would prevent the imposition of penalties, fines, or punishments under any state law against any bank for any act or omission which complies with any rule, regulation, interpretation, order, or approval of the Superintendent even if the act does not comply with other laws. Under this broad immunity, a bank might claim exemption from liability for discrimination in the hiring of employees for a new branch on the ground that the Banking Department had approved the opening of the branch, even though the application for approval did not disclose that the bank intended to engage in discrimination in hiring staff for that branch. There is simply no reason why the Financial Code should grant special exemptions to banks or trust companies from statutes which govern other types of businesses, including California's civil rights laws.

The Bill Weakens Current Law Governing Bank Branch Relocations

AB 2521 proposes to weaken the law governing changes in bank branch location.[49] It would allow all moves of a branch of less than two miles to be approved without any consideration of the impact on the public. In many parts of California, particularly those poorly served by public transit, a two-mile move could have a significant impact on the availability of services to a community. In Los Angeles, for example, this provision would allow the closing of a branch in a minority neighborhood near downtown Los Angeles and a reopening in the financial district, or a closing in predominantly low-income South Pasadena and a relocation to affluent Pasadena, without any consideration of the impact of the move on the community.

The bill also would allow a bank to claim that a branch closure is simply a "relocation" and thereby avoid the ninety-day notice requirement and the limited scrutiny required for branch closings. Although existing law defines a relocation as a change in location of less than two miles,[50] AB 2521 has no geographic limit on relocations. A bank which closes an office in East Los Angeles and opens one in Beverly Hills could call the change a "relocation".

The bill also would eliminate all regulation of the closing of automated teller machines.[51] Banks would not even have to give notice to customers before closing an ATM site.

The Standards for Scrutinizing the Effect of Branch Closures Are Inadequate

AB 2521 also fails to adequately protect bank customers from branch closures. The bill requires that notice regarding the closing of a branch must be given only *after* approval of the closing.[52] Notice is not very meaningful when it is given only after it is too late for customers to ask the Superintendent to deny approval of the closing. The bill would also make all branch closings automatically approved unless the Superintendent denies the application within thirty days.[53] Current law contains no such automatic approval provision, but instead permits the Superintendent broad discretion to deny an application to open or close a branch.[54] A thirty-day period is far too short to enable consumers to learn about and object to the proposed change. Moreover, approval should never be automatic, especially after there has been an objection.

Most importantly, the bill uses an unduly narrow standard for evaluating the impact of branch closures. It requires the Superintendent to approve every branch closure unless it would have a "seriously adverse effect" on the public.[55] Current Department regulations use the same language as the standard for the exercise of the Superintendent's discretion.[56] However, those regulations merely set guidelines for the exercise of the Superintendent's discretion and do not compel him or her to approve every branch closure which is harmful to the community but the level of harm is less than "seriously adverse." By contrast, AB 2521 states that the Superintendent must approve every proposed branch closure if he or she finds that there would not be a "seriously adverse effect"

on the public convenience and advantage.[57] This strict standard will severely limit the Superintendent's ability to protect underserved communities from further withdrawals by banks.

Banks should not be permitted to close branches indiscriminately. In 1983, there was one bank branch or office for every 5,200 Californians. By 1988, there was only one branch per 6,300 persons. Nearly three hundred bank branches or offices closed in California in those five years.[58] A bank which desires to close a branch in an underserved area should be required to prove that keeping the branch open will impair the bank's fiscal health. The bank should also be required to first offer the branch and its accounts for sale to any other financial institution which will take over the location and accounts and continue serving that community.

The Bill Would Allow Banks to Prevent Public Access to Information Filed with the Superintendent

AB 2521 would allow banks to prevent public access to a variety of information which banks and trust companies file with the Superintendent of Banking.[59] The bill permits a regulated bank or trust company to designate information which is to be treated as confidential. It requires the Superintendent to accept the bank or trust company's assertion of confidentiality without any showing of good cause or any independent determination of the need for confidentiality.[60] Reports which a bank has designated as confidential could not be disclosed to the public.[61] They also could not be disclosed in connection with a civil or administrative proceeding brought by persons other than the Superintendent or a federal banking agency. Many consumer statutes carry civil penalties and are enforced by law enforcement agencies or private attorneys general.[62] This section could deprive those law enforcement agencies acting to enforce consumer protection statutes civilly from access to information filed by a bank with the State Banking Department. The bill's bias in favor of secrecy is further revealed in provisions that would prohibit even the bank or trust company which filed the information with the Banking Department from waiving the privilege against disclosure.[63]

The Bill Would Require Some Depositors to Pay A Bank's Attorneys' Fees

Another example of the way AB 2521 is skewed in favor of banks and against consumers is its proposed revision of current law governing awards of attorneys' fees to prevailing consumers in suits regarding the adequacy of bank disclosure of account terms and conditions.[64] Existing law permits the award of attorneys' fees to a prevailing consumer in such suits but not to a prevailing bank.[65] The California Bankers Association proposes to change that section to one which would also permit a bank which wins a lawsuit brought by a depositor over the adequacy of disclosure of account terms to receive a court award requiring the consumer to pay the bank's attorneys' fees.[66] Needless to say, such a provision would have a chilling effect on a consumer's willingness to challenge a bank's disclosure practices, even if the consumer has a meritorious claim.

The Bill Would Eliminate Other Consumer Rights

The bill would also eliminate or reduce other consumer rights, including the right to withdraw a certificate of deposit or other insured time deposit without penalty if the deposit is sold to a new bank.[67] AB 2521 would eliminate that right for insured deposits.[68] A consumer who selects a particular bank with which to do business based upon that bank's location, personnel, or role in the community could suddenly find himself or herself in a deposit relationship with a bank which the consumer never chose. The bill would also eliminate existing language and type size requirements concerning notices owed to consumers when a bank seizes a customer's checking or savings account in payment for other debts owed by the customer to the bank under a so-called "banker's set-off."[69]

The bill would allow a bank to enforce contracts against minors, who are otherwise generally unable to contract.[70] It would expand the pool of persons who are bound by a current section creating a conclusive presumption that the consumer knew of an error in an account statement after a certain period of time.[71] It would eliminate the right of depositors to hold banks liable for their common law negligence in accepting an unauthorized check.[72] It would eliminate the six-month waiting period before a bank may open a safe deposit box and remove its contents for nonpayment of box rental fees.[73] These examples illustrate just some of the changes in law proposed by AB 2521 which directly reduce existing consumer rights.

THE CBA PROPOSAL FAILS TO ADDRESS SERIOUS AND LONGSTANDING CONSUMER PROBLEMS WITH THE BANKING INDUSTRY

The California Bankers Association's proposal utterly fails to address several serious and longstanding problems which California consumers have experienced with banks, including unaffordable checking accounts; refusal of banks to cash government checks for non-depositors; bank branch closings; lack of any ceilings on bank interest rates; and lack of any requirement that banks prove a record of good service to the community before the Superintendent of Banking gives them approvals to merge or expand.

Most Banks Refuse to Cash Government Checks for Non-Depositors

Most banks will not cash checks for persons without an account, yet according to the General Accounting Office, 75% percent of families receiving AFDC lack checking accounts. According to a recent report, 82% of 81 financial institutions surveyed throughout California refused to cash government checks for non-depositors at all, and 96% refused to do so free of charge.[74] Even those few financial institutions which did cash the checks often allowed branch managers the discretion to refuse to provide the service.[75] Californians without checking accounts are often forced to use high-cost non-bank check-cashing services. These services charge from 1-6% to cash government assistance checks, with an average charge of 2.15%.[76] On a $500 check, 2% is a $10 fee, and 6% is a $30 fee. Any new version of the banking law should require that banks which choose to accept government deposits must cash government checks for non-depositors without charge.

Consumers Need Low-Cost Checking Accounts

Consumers of low or modest income levels often cannot afford the monthly service charges and high minimum balance requirements of most checking accounts. One study showed that 53% of persons who used money orders could not afford a checking account, found the service charges too high, or could not accept minimum balance requirements.[77] Charges paid by bank customers rose 120% from 1978 to 1982 (from $4.9 billion to $10.8 billion).[78] High

checking account fees also have a disproportionate impact on minorities. One study showed that only 47% of minority families have checking accounts, as compared to 85% of white families.[79] The federal banking regulators have urged financial institutions to offer basic banking services at no or low cost.[80]

The fundamental characteristics of a basic checking account are ease of account opening and low cost to maintain. Such an account should, at minimum, have the following characteristics: no monthly fee or a fee of not more than $1 per month; no per-check or per-deposit charge for the first ten checks and the first three deposits per month; no minimum balance to open, and no minimum balance to maintain; and identification requirements which may be met by the low-income population. Any rewrite of the banking code should address this important consumer problem by requiring that state-chartered banks make available affordable basic accounts of this type.

Better Safeguards Are Needed to Protect Consumers From the Impact of Branch Closures

The problem of bank branch closures was addressed earlier in this article. In addition to the timing of notice and standard of approval issues already discussed there, any rewrite of the Financial Code should affirmatively and aggressively address the problem of underserved communities, possibly by requiring a bank which desires to close a branch to first offer the branch and its accounts for sale to any other financial institution which is willing to take over the location and accounts and continue serving that community. In addition, the Superintendent could be directed by law to identify those communities which are underserved and to deny permission for further branch closures in those areas unless the closure is necessary to preserve the financial soundness of the bank.

Consumers Deserve the Protection of An Interest Rate Ceiling

Most interest rates charged by banks in California are totally unregulated. AB 2521 proposes a broadening of the exemptions for bank subsidiaries from the anti-usury provisions of the California Constitution. State-chartered banks have charged Californians as much as 32-226% as an annual percentage interest rate. New York, by contrast, has a general ceiling on interest rates of 25%.[81] Any comprehensive banking bill should include a ceiling on consumer interest rates by banks and all other lenders of not more than 25% annual percentage interest rate.

Banks Should Prove That They Adequately Serve the Community Before Receiving Regulatory Approvals

Under the federal Community Reinvestment Act, federal agencies regulating depository institutions must consider "the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods..."[82] when they evaluate applications for transactions such as acquisitions, mergers, or new branches. Banks are subject to regulatory scrutiny concerning whether they have met these obligations each time they seek a variety of approvals from the federal banking regulators.[83] The State Superintendent of Banking should have the same power and obligation to examine a state-chartered bank's record of meeting community needs before the Department grants regulatory permission for sales, mergers, acquisitions, changes in branch location, waiver of regulations, or other regulatory approvals. A state banking charter is no less a privilege than a federal charter. Nonetheless, there is no provision in the state banking law which requires the Superintendent of Banking to consider the records of state-chartered banks before granting regulatory approvals. Thus, each section of the bill which deals with regulatory approvals should require the Superintendent to find, as a precondition for approval, that the applying bank has an excellent record of serving the deposit and lending needs of low- and moderate-income Californians, or has proposed a plan to do so.

CBA Has Not Shown a Need for a Comprehensive Rewrite of the California Banking Law

At the first informational hearing on AB 2521 held by the Assembly Finance and Insurance Committee and the Senate Banking Committee, bill authors and committee chairs Assemblymember Patrick Johnston and Senator Rose Ann Vuich called upon the California Bankers Association (CBA), as the sponsor of AB 2521, to explain why it believes that a substantial revision of the banking law is necessary. CBA responded by discussing the changes in the banking industry, such as new technology, which have occurred since the current code was written. However, CBA did not offer any reason why those technological changes require a complete revision of the Banking Law, nor did it point to any changes in the banking industry that compel the particular amendments proposed by CBA in AB 2521. CBA representatives talked about the benefits of a well-organized code, but the provisions of AB 2521 go far beyond simple renumbering or reorganization. CBA still has made no showing of need for such a broad rewrite of California's fundamental banking law.

CONCLUSION

The California Bankers Association has proposed sweeping changes in the division of the Financial Code governing banks, yet it has not shown a need for these changes. The serious problems and deficiencies in AB 2521 are a timely illustration of the principle that regulated industries should not write regulatory laws.

In her opening statement at the joint informational hearing, Senator Vuich called upon the California Bankers Association to address how this bill would benefit California consumers. Consumers Union believes that the unfortunate answer to this question is that the bill as presently drafted does not benefit and in fact harms consumers.

The legislature should decline to enact AB 2521 and rewrite the California Financial Code governing banks unless its provisions reducing consumer rights and weakening the effectiveness of the regulatory structure are removed, and affirmative provisions are added to address longstanding consumer problems with banks, including the issues of access to check cashing services by banks, access to affordable checking accounts, ceilings on interest rates, better scrutiny of branch closures, and stimulation of investment in low-income housing and community economic development.

AB 2521 authors Johnston and Vuich have stated that they plan to hold a series of public hearings on the bill to clearly identify those aspects of the bill which propose substantive changes and to fully explore the issues raised by these proposed changes. Those changes should be separated from the recodification aspects of the bill and rejected. If any bill which proposes substantive changes to the law governing banks is to move forward, that bill should also make changes which address important consumer problems.

FOOTNOTES

1. *Banking Bill Fails With Overseer,* Sacramento Bee, Aug. 24, 1989.
2. Financial Code § 200 *et seq.*
3. *Id.* § 2070 *et seq.*
4. *Id.* § 2050 *et seq.*
5. *Id.*
6. *Id.* § 500 *et seq.*
7. *Id.* §§ 3354-3356.
8. *Id.* § 3100 *et seq.*
9. Seventy-Eighth Annual Report of the Superintendent of Banks (1987), at 27.
10. However, the proposed changes in state law will also affect national banks. Federally-chartered banks frequently point to the powers granted to state-chartered banks by the states as a basis for proposed new powers or other changes in law. Also, AB 2521 would exempt national banks from certain pro-consumer provisions of the current Banking Law which now apply to national banks.
11. Seventy-Eighth Annual Report of the Superintendent of Banks (1987), at 56, 62.
12. *Id.* at 37.
13. *Id.* at 67.
14. The division of the Financial Code which the California Bankers Association proposes to rewrite also covers trust companies. Trust companies and trust departments of state-chartered banks managed $108.2 billion in assets in California in 1987. *Id.* at 64.
15. For over seventy years, courts have recognized the validity of banking regulation as an appropriate exercise of state police power due to the public interest nature of the industry. *See, e.g., Bank of Italy v. Johnson,* 200 Cal. 1 (1926); *State Savings and Commercial Bank v. Anderson,* 165 Cal. 437 (1913), *aff'd,* 238 U.S. 611 (1914); *Frankini v. Bank of America,* 31 Cal. App. 2d 666 (1939). Commentators generally agree that the intricate web of state and federal law regulating the banking industry is justified by several interrelated policy objectives: preservation of the safety and soundness of the banking system and of competition in banking; protection of consumers and stockholders; and the appropriate allocation of credit. *See, e.g.,* Scott, *The Patchwork Quilt: State and Federal Roles in Bank Regulation,* 32 Stan. L.R. 687 (1980). The community service obligations of banks are well recognized by Congress and the federal banking regulators. *See* 12 U.S.C. § 2901; Joint Policy Statement of the Federal Reserve Board, Office of the Comptroller of the Currency, Federal Home Loan Bank Board, and Federal Deposit Insurance Corporation on the Community Reinvestment Act, 54 Fed. Reg. 13,742 (1989).
16. AB 2521, proposed Financial Code § 203(c).
17. *See* Financial Code § 2050 *et seq.*; § 2070 *et seq.*
18. *Id.* § 703(b) (applications for acquisition of control of a bank or trust company); § 4855 (sale of a financial institution).
19. *See, e.g.,* AB 2521, proposed §§ 1302, 1406, 1425.
20. Federal Reserve Bank of San Francisco, Weekly Letter, *The California Deposit Rate Mystery* (Jan. 27, 1989).
21. Consumers Union, *Why Do California Banks Charge Consumers Up to 6% Higher Rates on Loans than Banks in Other States? Why do California Banks Pay Consumers as Much as 1.5% Lower Interest Rates on Their Deposits?* (Oct. 31, 1988).
22. Divestiture may be difficult to achieve under the antitrust laws. *See California v. American Stores Co.,* 872 F.2d 837 (9th Cir. 1989), *petition for cert. filed,* No. 89-258 (U.S. Aug. 10, 1989).
23. Financial Code § 703(b) (applications for acquisition of control of a bank or trust company); § 4855 (sale of a financial institution).
24. *Id.* § 703(a)-(g) (acquisition of control of a bank or trust company); *see also* § 4855(a)-(f) (setting forth similar standards for approval of a proposed sale).
25. AB 2521, proposed §§ 309, 1302, 1406, 1425.
26. *See id.*
27. *Id.,* proposed § 302.
28. *See, e.g., id.,* proposed §91 days to act on applications for acquisition of control); proposed § 302 (default period of 91 days).
29. *Id.,* proposed § 302.
30. *Id.,* proposed § 305.
31. Letter of August 15, 1989 to Assemblymember Patrick Johnston and Senator Rose Ann Vuich from James E. Gilleran, Superintendent of Banks, by Brian Walkup, Legislative Counsel, State Department of Banking, at 9.
32. AB 2521, proposed § 234.
33. *Id.,* proposed § 204(c).
34. Financial Code § 33202.
35. San Francisco Chronicle Special Report, Aug. 2, 1989, at A1.
36. AB 2521, proposed § 220.
37. Financial Code §§ 3354-3356.
38. AB 2521, proposed § 523(b)(2).
39. *Id.,* proposed § 115.
40. *Id.,* proposed §§ 3220-3224, 3207.
41. *Id.,* proposed § 4301.
42. *Id.,* proposed § 115.
43. *Id.,* proposed §§ 447, 3223.
44. The only immunity for banks in the current Banking Law is found in section 865.6, which provides a limited immunity for corrected errors in connection with deposits. That immunity, however, extends not more than sixty days after the time of the violation. It does not create an open-ended period for immunity until such time as the bank discovers its violation.
45. Civil Code § 51.
46. Business and Professions Code § 17500.
47. Business and Professions Code § 17200.
48. Certain federal statutes do have a provision to avoid liability for actions done in good faith conformity with that particular federal statute, but not for actions done in conformity with any other law. *See, e.g.,* 15 U.S.C. § 1640(b).
49. AB 2521, proposed §§ 2209, 2211; *compare* Financial Code §§ 503, 510.
50. Financial Code § 507.
51. AB 2521, proposed § 2202.
52. *Id.,* proposed § 2211. This same defect is present in current law, Financial Code § 510.
53. AB 2521, proposed §§ 2209(d), 302(a).
54. Financial Code § 503.
55. AB 2521, proposed § 2211.
56. 10 California Code of Regulations § 9951.
57. AB 2521, proposed § 2211.
58. State Department of Banking statistics provided to Consumers Union by telephone conversation (August 1989).
59. AB 2521, proposed §§ 415, 231.
60. *Id.*
61. At present, applications filed with the Department of Banking are exempt from disclosure under the Public Records Act, Government Code § 6254(d), but that act does not deprive the regulator of the discretion to make such documents available. AB 2521 would deprive the Superintendent of that discretion, and also would extend beyond applications to other types of materials filed with the Department by banks.
62. *See, e.g.,* Business and Professions Code §§ 17200, 17500.
63. AB 2521, proposed § 415(e).
64. *Id.,* proposed § 3223(e).
65. Financial Code § 865.6(e).
66. AB 2521, proposed § 3223(e).
67. Financial Code § 2051.
68. AB 2521, proposed § 1402.
69. *Id.,* proposed § 3207; *compare* Financial Code § 864.
70. AB 2521, proposed § 3201.

71. *Id.*, proposed § 3206; *compare* Financial Code § 861.

72. AB 2521, proposed § 3252; *compare Sun N' Sand, Inc. v. United California Bank,* 21 Cal. 3d 671, 695-700; 148 Cal. Rptr. 329, 346-49 (1978).

73. AB 2521, proposed § 3303.

74. *See, e.g., Consumer Action News, Banking Information Series* (Aug./Sept. 1989).

75. *Id.*

76. *Check Cashing in California,* survey released by the Office of Assemblymember Peter Chacon (Mar. 11, 1988).

77. *The Money Order User Profile,* researched by J. Maclachlan and Associates (Apr. 1985).

78. *See Smaller Customers Get Less Service at Banks and Pay More Charges,* Wall St. J., Oct. 18, 1984, at 1.

79. *Bank Service Charges and Fees: Their Impact on Consumers,* Federal Reserve Study (1983).

80. OCC Banking Circular Re: Basic Banking Services (Aug. 23, 1985).

81. N.Y. Penal Code § 190.40.

82. 12 U.S.C. § 2903.

83. *Id.*