Daily Journal Newswire Articles
www.dailyjournal.com
© 2009 The Daily Journal Corporation. All rights reserved.

FORUM (FORUM & FOCUS) • Jun. 30, 2009

The Case Against Consolidation

FORUM COLUMN

By Keith Paul Bishop

One hundred years ago, committees of the California Bankers' Association, the California Legislature and the Commonwealth Club of San Francisco tackled the problem of how the state regulated banks. A weak and understaffed board of commissioners had not proven to be up to the task. The result of the committees' work was the enactment of the Banking Act of 1909. The new act was based on the premise that banking regulation would be more effective if it was overseen by a single official, the superintendent of banking, and a staff of expert examiners.

Two years later, the state of Kansas adopted the first state securities, or blue sky, law, to protect investors. Shortly thereafter, California Gov. Hiram Johnson happened to discuss the law with Kansas' Gov. Walter Roscoe Stubbs. Apparently, Johnson like what he heard. The result was California's first securities law - the Investment Companies Act of 1913. Like its older brother, the Banking Act, the Investment Companies Act established oversight by a single official, the commissioner of corporations, and an expert staff.

In the ensuing century, each of these departments has served the public well. Although the Department of Banking was renamed the Department of Financial Institutions in 1997, the original banking act's fundamental principles of centralized oversight and expert staffing remain. Although securities laws were modernized over the years, the Department of Corporations has been for many decades a recognized leader in state securities regulation. Today, however, the proud traditions of these two departments are in jeopardy. The Legislature is considering a proposal, AB 33 (Nava), to eliminate their independent existences. In their place, the Legislature is proposing the creation of a new department to be called the Department of Financial Services. The powers and functions of the Departments of Banking and Corporations would transferred to new divisions in the Department of Financial Services.

I served as one of California's commissioners of corporations and before that as an interim savings and loan commissioner. In these positions, I was responsible for the administration and enforcement of both securities and financial services laws. I have also served as deputy secretary for business regulation and general counsel to the California Business, Transportation & Housing Agency. In that capacity, I worked with the leadership and staffs of both the Department of Banking and the Department of Corporations. Enactment of AB 33 would be a profound mistake. I am not alone in this view. Five former commissioners, superintendents and chief deputies of the Departments of Banking and Financial Institutions have signed a letter voicing their "strong" opposition to AB 33. The Financial Institutions Committee of the Business Law Section of the California State Bar is opposed to the bill.

I am opposed to AB 33 for several reasons. First, the Departments of Financial Institutions and Corporations administer and enforce laws that have fundamentally different objectives. Although both departments are generally concerned with regulating financial services, the industries that they regulate are completely different. The Department of Financial Institutions primarily regulates banks and credit unions. Although there are significant differences between these two types of institutions, they share the common element of being depository institutions. The basic objective of any regulator of depository institutions is to ensure the "safety and soundness" of those institutions for the protection of their depositors and ultimately the economy as a whole. The Department of Financial Institutions has an experienced staff that is trained and focused on its mission of ensuring the safety and soundness of its licensees.

In contrast, the Department of Corporations currently does not administer laws governing depository institutions per se. Thus, its regulatory focus has been in different areas. For example, the Department of Corporations administers and enforces the Corporate Securities Law of 1968 and the Franchise Investment Law. The principal purpose of both of these laws is to protect investors. Although the Department of Corporations regulates finance lenders and residential mortgage lenders, neither of these types of business take deposits. Thus, neither the California Finance Lenders Law nor the Residential Mortgage Lending Act is grounded on the principle of ensuring safety and soundness in the same manner as the banking law.

Consolidation of the departments will not result in either streamlining or simplifying regulatory oversight. An application to be licensed as a bank has almost nothing in common with an application for a permit to offer and sell securities. Thus, consolidating the supervision of these laws within a single regulator will not simplify or streamline the licensing processes currently in place. Changing the regulator at the top will not change the substantive requirements for a license or the rules governing the operation of licensees. While the creation of the Department of Financial Services will give the outward appearance of a "one-stop" regulator, the reality will be that the department will be internally organized along virtually the same lines as the Departments of Financial Institutions and Corporations are today.

Nor will consolidation improve the efficiency of regulation. The staffs of the Departments of Financial Institutions and Corporations are well trained and experienced. This does not mean that they are fungible. A bank examiner cannot be immediately turned into a securities regulator (or vice versa). Because the training and experience the staffs of these departments differ so significantly, no real efficiencies can be realized by housing them under a single regulator. In fact, consolidation would likely dilute regulatory focus and efficiency.

Consolidation will likely disrupt the existing regulatory programs. Any consolidation would result in significant disruptions. Presently, the California economy is facing unprecedented stresses. At this critical time, regulators should not be distracted by regulatory consolidation.

No significant cost savings have been identified. According to the Assembly Appropriations Committee, there are "unknown potential long-term savings." These savings would only be realized if there are more streamlined services and operating efficiencies. There is very little opportunity for either streamlining services or improving operating efficiencies. In any event, both the departments are special fund agencies that are supported by licensee fees and assessments rather than the General Fund. Licensees already demand cost efficient regulation from their existing regulators.

The Departments of Financial Institutions and Corporations have served the people of California well through a century of wars, depression and economic bubbles. Their accumulated experience and expertise should not be diluted at this critical time. There is simply too much at stake to risk a loss of focus and expertise.

Keith Paul Bishop is a partner in the Irvine office of Allen Matkins Leck Gamble Mallory & Natsis and an adjunct professor at the Chapman University School of Law.

****

© 2009 Daily Journal Corporation. All rights reserved.