



CALIFORNIA  
**BANKERS**  
ASSOCIATION

May 18, 2020

Department of Business Oversight  
Attn: Regulations Coordinator  
1515 K Street, Suite 200  
Sacramento, CA 95814-4052

Re: Invitation For Comments On Proposed Rulemaking Public Banking Law: Definitions and Application Requirements (Pro 1/20) Proposed Rulemaking

Dear Madam or Sir:

The California Bankers Association (“CBA”) writes this letter on behalf of the depository financial institutions doing business in the state of California. CBA, established in 1891, is a division of Western Bankers Association, a professional non-profit organization for banks doing business in 13 western states and 3 U.S. territories.

This letter addresses the Invitation For Comments On Proposed Rulemaking Public Banking Law: Definitions And Application Requirements (Pro 1/20) (the “Invitation”), which established a process for a local agency to apply for a public bank charter from the Department of Business Oversight (“DBO”) as authorized by AB 857 (Chapter 442, Statutes of 2019).

CBA opposed this legislation because, among other things, we believe a public bank funded by taxpayer money puts California’s financial health at risk and is fiscally irresponsible, a consideration made even more significant as a result of the COVID-19 impacts on our state. And we remain opposed to the regulatory efforts to create a public bank. The Invitation has highlighted and reinforced the systemic risks of creating a public bank and the multitude of complex issues that will need to be addressed in the rulemaking process. While we do offer feedback on some of the questions asked, we decline to offer comments in areas where the responsibility to assure the safety and soundness of the banking system within California lies exclusively with the department as regulator, therefore our comments should not be considered exhaustive. We respect the role the DBO has in developing and implementing these regulations and the duty it has in approving/reviewing a bank’s application to ensure a safe and sound banking system in California.

We appreciate the opportunity to provide comments on this rulemaking process. The invitation for comment by the Commissioner asks for input in developing regulations to clarify certain definitions and the application requirements to organize and establish a public bank.

## **Definitions**

The Invitation indicates that AB 857 introduced terms relating to public banking and that not all of these terms are defined. Specifically, the following terms are identified for feedback:

### *1. Jurisdiction of the Public Bank*

CBA believes that the jurisdiction of a public bank should refer to a geographically defined boundary. As such, a city's jurisdiction should encompass that city's current incorporated geographical boundary, a county's jurisdiction should consist of the geographic boundary of that governmental unit, and the geographical boundaries of any local agencies or joint powers authority should encompass these entities jurisdictions as well.

### *2. Local Financial Institution*

We believe that a "local financial institution" should be a geographically defined boundary that is within the jurisdiction of the public bank as set out in the above answer. Thus, a local financial institution should be geographically located within the jurisdiction of the public bank.

### *3. Compete, Offered and Provided, and Financial Products and Services*

The Invitation states that the central issue that determines whether a financial product or service "competes" with one offered by a local financial institution is dependent on how "financial products or services" is defined. CBA believes that financial products and services should be defined as the actual product or service level and not by the terms level. Allowing a public bank to offer the same product or service as a local financial institution but at a different term level defies the express language contained in Government Code Section 57604 prohibiting this activity as well as the clear legislative intent of AB 857 for public banks not to compete with a local financial institution.

### *4. Governing Board of a Public Bank and Designated Alternate Member*

CBA believes that governing board of a public bank should have the same meaning as a board of directors. Regarding the definition of a designated alternative member, this definition should require that any alternate member should also be a member of the governing entity that created the public bank.

### *5. Organizers*

As to who should be considered an organizer of a public bank, organizers must meet the same requirements as organizers of a state or federally chartered commercial bank including, but not limited to, the following minimum requirements: requisite banking knowledge and experience, thoroughly vetted background check that establishes each organizer's responsibility, honesty, integrity, and, in lieu of capital contributions to the public bank, the placement of bonds for each individual organizer and/or board member in an amount sufficient to protect the public bank against a public officials malfeasance or negligence.

## Application Requirements

Generally, a local agency seeking to establish a public bank should at a minimum be required to undergo the same scrutiny and examination as other entities would undergo in the formation of a financial institution.

### 1. *Character of Organizers*

Organizers of a public bank should be explicitly subject to the same requirements as organizers of private banks as required under Financial Code section 1022. As such, the Commissioner should make a careful investigation and examination into the character, reputation, and financial standing of the organizers or incorporators and their motives in seeking to organize the proposed bank.

### 2. *Reasonable Promise of Successful Operation*

Financial Code section 1023 requires the Commissioner to ascertain that a proposed bank will have a reasonable promise of successful operation prior to approving an application for a license. At a minimum, this factor should be interpreted the same for a public bank and we would argue that since a public bank is being formed with public funds a higher fiduciary standard should apply to ensure that taxpayers of a governmental entity forming a public bank are protected from potential misguided or misinformed decisions.

### 3. *Viability Study*

In general, we believe that a viability study should include a determination of whether the applicants are of good character, whether a necessity exists in the community for the public bank, whether there is a reasonable probability for the bank's usefulness and success, whether the public bank can be established without undue harm to existing financial institutions, whether there is competent management with experience requisite to the type of services and products to be provided, and will be operated in a safe and sound manner.

#### i. Estimate of Initial Amount of Capital

As part of the viability study that a local agency shall conduct prior to the formation of a public bank, we believe that the information regarding proposed capitalization contained in CCR Section 10.3167 requiring a pro forma statement of the shareholders' equity of the subject institution as of the date of commencement of business and describing the plan for selling shares of the subject institution should be required as part of a public bank viability study.

#### ii. Financial Projections

CBA believes that the financial projections requirement of the viability study should at a minimum contain the information regarding proforma financial statements requirements contained in CCR Section 10.3168. We would argue that the standards for a public bank that is

entrusted with public funds should be held to a higher standard and both the pro forma balance sheet and pro forma statement of income requirements should reflect that.

iii. Corporate Governance

As the Commissioner is considering requiring the corporate governance requirement of the viability study to include a proposed policy against self-dealing, insider transactions, and conflict of interests, we agree that this provision is not only reasonable but necessary to ensure that needed protections exist.

4. *Control Persons*

Any individual or entity that the Department determines, in the exercise of its regulatory powers to ensure safety and soundness of the public bank, to be a control person must be evaluated and assessed in the same manner and to the same extent as a proposed control person for a state or federally chartered commercial bank under existing federal and state laws and regulations.

5. *Corporate Structure*

CBA declines to offer comment at this time about corporate structure other than to note that any “member” or “shareholder” should be subject to the same regulatory scrutiny and responsibilities as those imposed upon a “shareholder” of a state or federally chartered institutions under existing law. In addition, CBA recommends that such individuals or entities be subject to the bonding requirements set forth above (See, subdivision 5 of the Definitions section, supra) for so long as the individual or entity is a part of the public bank’s corporate structure.

CBA appreciates the opportunity to participate in this comment process and we look forward to our continued work with your Department through the additional rulemaking phases to implement this new law.

Sincerely,

CALIFORNIA BANKERS ASSOCIATION

By: Mike Webb  
Mike Webb  
Vice President, Assistant General Counsel