



Americans in 1991, yet still rejected more than two-thirds of minority applicants for home loans in the same year. The bank reported that it rejected 67.5% of minority applicants for home mortgages in 1991, compared to 55% of white applicants. Throughout the state, minorities continue to be rejected for mortgages at a much higher rate than whites, although that statistic also seems to be improving. BankAmerica denied 1.5 loan applications for African-Americans and Latinos for every one application from whites denied in 1991. This figure is down from the 1.6:1 ratio in 1990.

While the recession may be partly to blame for minorities' plight in obtaining loans, and while California banks seem to be showing some signs of decreasing the lending gap, there is room for much improvement. "We're pleased that we showed progress in 1991, but we are not satisfied. We believe we can do better," said BankAmerica Executive Vice President Donald Mullane. James Ketcham, a senior vice president of Wells Fargo's mortgage division, stated, "In a nutshell, we are not happy with the level of activity that Wells Fargo has in minority communities." The spotlight will be on lenders in 1993, as minority and low-income groups and advocates watch to see whether bankers follow through with their stated plans to decrease the minority lending gap.

**BofA/Security Pacific Merger Update.** In August 1991, two leading banks in California, BankAmerica Corporation and Security Pacific, announced their intention to merge into one financial service giant; the new bank is called BankAmerica. [11:4 CRLR 123] After the merger, which occurred in April 1992, BankAmerica had a total of 1,440 branches statewide. In November, the company announced that 450 of those offices, the majority in southern California, will be closed over the next eight months. According to BankAmerica officials, southern California will bear the brunt of the closures because of the close proximity of many former Security Pacific and BofA offices; in such instances, the majority of closures will be the Security Pacific branches. Experts estimate that the closures will result in the loss of approximately 9,000 jobs statewide.

**SBD Releases Third Quarter Report.** In December, SBD released its quarterly report covering the third quarter of 1992. According to SBD, at the close of business on September 30, the 262 state-chartered banks with 1,818 branch offices had total assets of \$111.1 billion, an increase of \$2.9 billion, or 2.7%, from September 30, 1991. From September 30, 1991, to September 30, 1992, the state experienced a

net decrease of ten banks and a net increase of 61 branch offices.

**Cease and Desist Warnings Issued.** On November 6, the Superintendent of Banks issued a warning to cease and desist doing business in California without a license to John H. Thaler, Industrial Bank of Kibris, Ltd., United States Representative Office, and Premier Bancorp, Inc., all of Beverly Hills. Recently, a number of cashier's checks were issued by the Industrial Bank of Kibris, U.S. Representative Office, which bear the signature of John H. Thaler. SBD is asking that all persons who have communicated with Thaler, the Industrial Bank of Kibris, U.S. Representative Office, or Premier Bancorp, Inc., contact its legal division in Los Angeles. SBD noted that Premier Bancorp, Inc., is not affiliated in any way with Premier Bank, which is licensed by the Superintendent of Banks to conduct banking business, is headquartered in Northridge, and maintains branch offices in Thousand Oaks and Warner Center.

**Interim Guidance Concerning Restrictions on Activities of FDIC-Insured State Banks.** On November 27, the FDIC issued interim guidelines on the implementation of the federal FDIC Improvement Act of 1991. That Act added new section 24 to the Federal Deposit Insurance Act, which generally limits the activities and equity investments of insured state banks and their subsidiaries to those permissible for national banks and their subsidiaries. The FDIC adopted final regulations implementing the equity investment restrictions on November 13, but is still in the process of developing regulations to implement the activity restrictions of section 24, which became effective on December 19. Thus, the FDIC provided the following interim guidelines until its final regulations are adopted.

Under section 24, an insured state bank may not directly or indirectly through a subsidiary engage as principal in any activity that is prohibited for a national bank unless specifically excepted in section 24 or the FDIC gives its consent for the bank or its subsidiary to engage in the activity. A state-chartered bank that is, as of December 19, engaging in such a prohibited activity should seek interim approval to continue the activity by writing to the appropriate FDIC Division of Supervision (DOS) regional office. A state-chartered bank that is not, as of December 19, engaging in such an activity but wishes to receive approval should similarly contact the appropriate DOS regional office. A bank that is unsure whether a particular activity is permissible for a national bank should first seek the advice of its counsel

and then contact the appropriate DOS regional office. The FDIC will not take enforcement action against a bank that continues to engage in an impermissible activity without receiving the necessary temporary approval provided the bank is was acting in good faith based on an opinion of counsel.

**Superintendent Participates in International Conference.** In November, SBD Superintendent James Gilleran attended the International Conference on Russian Banking held in Moscow. Gilleran, who attended in his capacity as a representative of the Conference of State Bank Supervisors, participated in panels discussing the organization, structure, regulation, and supervision of the banking industry in the United States. According to SBD, the Russian banking system has had significant expansion during a very short period of time, currently having 1,600 new commercial bank charters.

## DEPARTMENT OF CORPORATIONS

*Commissioner: Thomas Sayles*  
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**T**he Department of Corporations (DOC) is a part of the cabinet-level Business, Transportation and Housing Agency and is empowered under section 25600 of the California Code of Corporations. The Commissioner of Corporations, appointed by the Governor, oversees and administers the duties and responsibilities of the Department. The rules promulgated by the Department are set forth in Chapter 3, Title 10 of the California Code of Regulations (CCR).

The Department administers several major statutes. The most important is the Corporate Securities Act of 1968, which requires the "qualification" of all securities sold in California. "Securities" are defined quite broadly, and may include business opportunities in addition to the traditional stocks and bonds. Many securities may be "qualified" through compliance with the Federal Securities Acts of 1933, 1934, and 1940. If the securities are not under federal qualification, the commissioner must issue a "permit" for their sale in California.

The commissioner may issue a "stop order" regarding sales or revoke or suspend permits if in the "public interest" or if the plan of business underlying the securities is not "fair, just or equitable."



## REGULATORY AGENCY ACTION

The commissioner may refuse to grant a permit unless the securities are properly and publicly offered under the federal securities statutes. A suspension or stop order gives rise to Administrative Procedure Act notice and hearing rights. The commissioner may require that records be kept by all securities issuers, may inspect those records, and may require that a prospectus or proxy statement be given to each potential buyer unless the seller is proceeding under federal law.

The commissioner also licenses agents, broker-dealers, and investment advisors. Those brokers and advisors without a place of business in the state and operating under federal law are exempt. Deception, fraud, or violation of any regulation of the commissioner is cause for license suspension of up to one year or revocation.

The commissioner also has the authority to suspend trading in any securities by summary proceeding and to require securities distributors or underwriters to file all advertising for sale of securities with the Department before publication. The commissioner has particularly broad civil investigative discovery powers; he/she can compel the deposition of witnesses and require production of documents. Witnesses so compelled may be granted automatic immunity from criminal prosecution.

The commissioner can also issue "desist and refrain" orders to halt unlicensed activity or the improper sale of securities. A willful violation of the securities law is a felony, as is securities fraud. These criminal violations are referred by the Department to local district attorneys for prosecution.

The commissioner also enforces a group of more specific statutes involving similar kinds of powers: Franchise Investment Statute, Credit Union Statute, Industrial Loan Law, Personal Property Brokers Law, Health Care Service Plan Law, Escrow Law, Check Sellers and Cashers Law, Securities Depositor Law, California Finance Lenders Law, and Security Owners Protection Law.

A Consumer Lenders Advising Committee advises the commissioner on policy matters affecting regulation of consumer lending companies licensed by the Department of Corporations. The committee is composed of leading executives, attorneys, and accountants in consumer finance.

### MAJOR PROJECTS

**Crackdown on Unregistered Franchisors.** In an October 30 news release, DOC announced that Commissioner Thomas Sayles had issued desist and refrain orders for unregistered offerings of

franchises to residents of California to the following companies and individuals: Wood-Revivers of Alamo, California and its president Michael Deffina; National Safety Associates, Inc. of Memphis, Tennessee and its president Jay Martin; ACI Franchising Group, Inc. of Los Angeles, its president Alex Parsinia, and affiliate Allied Corporate Franchising Group, Inc.; and MOST Business Center c/o Management Design Services of San Francisco. According to DOC, the orders resulted from consumer complaints and the Department's efforts to inspect business and franchise expositions to ensure compliance with the California Franchise Investment Law, which requires franchisors to register their franchises with DOC or qualify for an exemption from registration prior to any offer or sale in California.

In the news release, the Commissioner urged members of the public to make sure they are dealing with a registered franchisor so that they will get complete disclosure regarding the financial condition and experience of the franchisor, as well as any support services the franchisor will provide. Before entering into a franchise agreement, interested investors may contact DOC to determine if the business opportunity is a registered franchise or has qualified for an exemption, and whether any public enforcement action has been taken by the Commissioner against the company, its principals, or sales personnel; they may also contact the California Department of Justice (DOJ) to see if DOJ has taken any action against the business and if the business is registered as a Seller Assisted Marketing Plan.

The Franchise Investment Law requires the franchisor to give prospective franchisees a list of existing franchisees; the Commissioner advised all potential franchisees to contact any such existing franchisees for more information about the franchisor. DOC noted that investors may also wish to consider retaining an attorney or other financial professional who practices in the area of franchising to assist them in reviewing a transaction to determine whether a franchise is involved and whether it is viable.

A brochure entitled *Should I Buy This Franchise? A Checklist for Prospective Investors* is available from DOC.

**Vacancies on the Escrow Law Advisory Committee.** In October, DOC announced that the Commissioner is seeking to fill vacancies on the Escrow Law Advisory Committee, which assists the Commissioner in the implementation of the Escrow Law. Effective January 1, the Escrow Law Advisory Committee has vacancies for the following positions: an at-

torney experienced in escrow matters; a representative of a medium-sized escrow business; and a representative of a different type of business ownership. The eleven-member Committee meets at least quarterly; its members are appointed by the Commissioner and serve for a two-year term without compensation or reimbursement for expenses. DOC accepted applications until November 16.

**Regulatory Action Under the Health Care Service Plan Act.** On September 14, the Office of Administrative Law (OAL) approved DOC's repeal of sections 1300.63.50, 1300.64.50-1300.64.55, 1300.67.50-1300.67.53, and 1300.67.55-1300.67.59, Title 10 of the CCR, DOC's extensive regulations governing Medicare supplemental insurance. The Department's actions were necessitated by the enactment of SB 925 (Torres) (Chapter 287, Statutes of 1992), which enacted comprehensive guidelines to regulate health care service plan contracts which supplement Medicare, and which incorporated DOC's regulations.

**Regulatory Action Under the Credit Union Law.** On November 13, the Commissioner published notice of his intent to amend section 976, Title 10 of the CCR, which implements the Credit Union Law. According to DOC's informative digest, many in the credit union industry, as well as DOC staff, have difficulty understanding existing section 976(c), which sets forth exemptions from the calculation of the 40% limitation on real estate lending. Also of concern is section 976(b)(3), which is referenced in section 976(c) and which provides an exclusion from the general requirement that loans secured by real estate may not exceed 40% of a credit union's total loan portfolio.

Thus, the Commissioner proposes to amend the introductory paragraph in section 976(b)(3) to clarify the existing language. The Commissioner also proposes to rewrite section 976(c) by redrafting and rearranging one complex compound-sentence into shorter, simple sentences. Essentially, the complex sentence states that any loans meeting certain federal standards and saleable in the secondary market or any loans written in accordance with paragraphs (A), (B), or (C) of section 976(b)(3) are excluded from the 40% limitation provided that the credit union meets certain standards. The Commissioner proposes to rewrite this sentence to state that credit unions meeting certain standards may exclude from the 40% limitation certain types of loans. The Commissioner received public comment on these proposals until January 8; no public hearing is scheduled at this writing.



In other DOC rulemaking under the Credit Union Law, OAL approved the Department's amendment to section 922, Title 10 of the CCR, on December 16. The amendment authorizes California-chartered credit unions to invest in mutual funds or trusts provided that all investments and investment practices of the mutual funds or trusts would be permissible if made directly by the credit union or federal credit unions. [12:4 CRLR 141]

At this writing, DOC is still reviewing the comments received on its proposal to repeal existing section 909 and adopt new section 909, Title 10 of the CCR; new section 909 would clarify when bond or insurance coverage is deemed "commensurate with risks involved." [12:2&3 CRLR 166]

**Regulatory Action Under the Corporate Securities Law.** Pursuant to Corporations Code section 25105, the Commissioner of Corporations may exempt by rule any transaction which is not within the purpose of the Corporate Securities Law of 1968 and the qualification of which is not necessary or appropriate in the public interest or for the protection of investors. Currently, Rule 144A of the Securities and Exchange Commission (17 C.F.R. Part 230.144A) provides a safe harbor exemption from the regulation requirements of the Securities Act of 1933 for certain offers to resell or resales to specified qualified institutional buyers. In addition, the fact that purchasers of securities from the issuer thereof may purchase restricted securities with a view to reselling those securities pursuant to Rule 144A does not affect the availability to the issuer of an exemption under section (4)(2) of the Securities Act of 1933 or Regulation D under that Act.

On November 13, the Commissioner published notice of his intent to add section 260.105.13 to Title 10 of the CCR, to provide an exemption from the provisions of Corporations Code section 25130 for any offer to resell or resale of restricted securities made in compliance with Rule 144A of the Securities and Exchange Commission. Additionally, the Commissioner proposes to add section 260.102.10.1 to Title 10 of the CCR, to clarify that the offer to resell or resale made under section 260.105.13 constitutes an allowable distribution of securities by a purchaser under Corporations Code section 25102(i). Similarly, the Commissioner is proposing to add section 260.102.15 to Title 10 of the CCR to clarify that the offer to resell or resale made under section 260.105.13 constitutes an allowable distribution of securities by a purchaser under Corporations Code section 25102(f)(3). The Commis-

sioner received public comment on the proposals until January 8; no public hearing is scheduled at this writing.

AB 3763 (Mays) (Chapter 884, Statutes of 1992) created a modified permit application process for small companies intending to raise up to \$1 million in any twelve-month period through the offer and sale of securities to the public. This special permit process is available to California corporations or foreign corporations transacting business in California which are operating companies not engaged in highly speculative businesses such as oil and gas exploration or production, mining, or other extractive industries.

The type of security that may be offered by these small companies under the modified review and approval process is limited to one class of voting common stock, and there must be only one class of voting common stock immediately after the proposed sale and issuance. A minimum offering price of \$5 per share is also required, and the net proceeds from the offering are to be expended in the operations of the business. In addition, the offering is to be made pursuant to a special disclosure document based on the Form U-7 disclosure document developed for small companies by the North American Securities Administrators Association (NASAA), with such additional requirements as the Commissioner shall prescribe, including but not limited to investor suitability and due diligence investigation requirements. The application and disclosure document must be reviewed and signed by each member of the board of directors of the applicant. Finally, AB 3763 amended Corporations Code section 25608 to provide that the fee for filing a small company permit application under Corporations Code section 25113(b)(2) is \$2,500; an additional fee of up to \$1,000 may be charged a small company applicant where the actual costs of processing the application exceed the \$2,500 filing fee.

On November 27, in order to implement AB 3763, the Commissioner published notice of his intent to amend sections 260.110, 260.110.2, and 260.113 and adopt new section 260.113.1, Title 10 of the CCR. Proposed amendments to section 260.110 would allow a small company application for qualification under California Corporations code section 25113(b)(2); specify instructions concerning the signature of the small company application form; and specify the appropriate filing fee for that application. Proposed amendments to section 260.110.2 would require an application under Cor-

porations Code section 25113(b)(2) to be signed by each member of the small company applicant's board of directors. Proposed revisions to section 260.113 would require a small company applicant to attach and incorporate a copy of the Small Company Offering Registration Form; require the applicant to file an undertaking that there will be no stock splits, stock dividends, spinoffs, or mergers for a period of two years from the close of the offering; and replace existing references to the California Administrative Code with references to the CCR. Proposed new section 260.113.1 would specify the Small Company Offering Registration Form (Form C-7) based on the Form U-7 as adopted by NASAA, and such additional requirements as prescribed by the Commissioner.

Additionally, Corporations Code section 25613 authorizes the Commissioner to prescribe the form and content of financial statements required under existing law, and the circumstances under which such financial statements must be filed and audited by an independent certified public accountant; section 260.613, Title 10 of the CCR, sets forth those requirements with respect to financial statements. DOC proposes to amend section 260.613 to require statements of income and statements of cash flow, specify circumstances under which audited financial statements shall not be considered unqualified, and clarify the circumstances under which financial statements filed with the Securities and Exchange Commission shall satisfy the requirements of the rule.

The Commissioner received public comment on these proposed regulatory changes until January 18; no public hearing is scheduled at this writing.

In other DOC rulemaking under the Corporate Securities Law, OAL approved the Department's amendments to sections 260.101.1 and 260.101.3, Title 10 of the CCR, on December 4. These amendments enable the National Association of Securities Dealers, Inc. to file a notice of exemption on behalf of an issuer whose securities meet the requirements of Corporations Code section 25101(b)'s exemption, and facilitate the exemption notice filing by enabling the use of computer tape or disk. [12:1 CRLR 113]

Finally, DOC is still reviewing comments received in response to its proposal to amend section 260.105.11, Title 10 of the CCR, limiting the exemption for non-issuer trading of foreign-country issuer securities. [12:2&3 CRLR 165]

**DOC Rulemaking Under the Franchise Investment Law.** On December 24, the Commissioner announced his intent to



adopt proposed changes to the Department's regulations under the Franchise Investment Law.

Section 310.100.2(a), Title 10 of the CCR, regarding the negotiated sale of a franchise, provides an exemption from the registration requirement of Corporations Code section 31110 for the offer and sale of a franchise and allows the sale of a franchise if certain conditions are met. The first condition—codified in subsection 310.100.2(a)(1)—requires the initial offer to be the offer registered under Corporations Code section 31111; the Commissioner proposes to amend this subsection and expand the exemption to include renewed and amended registrations. The Commissioner also proposes to modify the second condition—codified in subsection 310.100.2(a)(2)—to require the franchisor to reasonably assume that the prospective franchisee has the business or financial experience to be able to protect its own interests in connection with the transaction.

The Commissioner additionally proposes to delete the rest of the existing conditions in section 310.100.2, on the basis that franchisors sometimes use the provisions in the rule as an excuse for refusing to negotiate terms with a franchisee. As a consequence, the intent of the rule (to encourage some flexibility with respect to the offer and sale of the terms of a franchise) is undermined. Instead, the Commissioner proposes to adopt language in subsection (a)(3) which will require (1) that the franchisor amend its registered offer prior to selling the franchise to disclose which items have been negotiated with other franchisees, and (2) that the franchisor attach to the offering circular all notices filed in California during the past 12 months, if the negotiated sale was made within 12 months of the offer being made.

Section 310.114.1 sets guidelines for the preparation of the offering circular. The Commissioner proposes to amend section 310.114.1(b) to include guidance on how to describe the franchisee and the franchisor(s) in the offering circular; amend subsection 310.114.1(c), which contains special instructions for the Uniform Franchise Registration Application ("UFOC") to reflect the application of the instruction sheet to California transactions only; and amend UFOC instructions 1, 2, 3, and 5.

The Commissioner scheduled no public hearing on these regulatory changes; at this writing, written comments are accepted until February 12.

## LITIGATION

After nearly two months of testimony and legal arguments, the federal criminal trial against former savings and loan boss Charles Keating and his son Charles Keating III on charges of racketeering, bank and securities fraud, and the interstate transportation of stolen goods went to the jury in late December; the charges stem from the \$2.6 billion collapse of Lincoln Savings and Loan, and its parent company, American Continental Corp. (ACC), both owned by Keating. A 77-count federal indictment alleges that the two Keatings and three other officers of Lincoln and ACC, who have entered into a plea bargain, created sham profits for ACC through fraudulent sales of undeveloped land, and sold ACC junk bonds based on those false profits. The Keatings, who have pleaded innocent, face up to 510 years in prison if convicted on all 77 counts, as well as fines of \$17 million and forfeiture of assets up to \$250 million. The elder Keating is already serving a ten-year state court sentence for defrauding 25,000 investors out of \$268 million by persuading them to buy worthless junk bonds instead of government-insured certificates. [12:4 CRLR 144]

Last July, in one of the numerous civil lawsuits stemming from Lincoln's failure, a federal jury ordered Keating and three co-defendants to pay over \$3 billion in damages for conspiring to defraud investors; specifically, the jury awarded the 20,000 class action plaintiffs \$600 million in compensatory damages and \$1.5 billion in punitive damages from Keating, and \$1.4 billion in compensatory damages and \$900 million in punitive damages from Keating's three co-defendants. [12:4 CRLR 144] However, in October U.S. District Judge Richard M. Bilby reduced the total award to approximately \$1 billion, cutting the total compensatory damages to \$288.7 million, dismissing the punitive damages against all defendants except Keating, and reducing punitive damages against Keating to \$750 million.

## DEPARTMENT OF INSURANCE

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Insurance is the only interstate business wholly regulated by the several states, rather than by the federal government. In

California, this responsibility rests with the Department of Insurance (DOI), organized in 1868 and headed by the Insurance Commissioner. Insurance Code sections 12919 through 12931 set forth the Commissioner's powers and duties. Authorization for DOI is found in section 12906 of the 800-page Insurance Code; the Department's regulations are codified in Chapter 5, Title 10 of the California Code of Regulations (CCR).

The Department's designated purpose is to regulate the insurance industry in order to protect policyholders. Such regulation includes the licensing of agents and brokers, and the admission of insurers to sell in the state.

In California, the Insurance Commissioner licenses approximately 1,300 insurance companies which carry premiums of approximately \$63 billion annually. Of these, 600 specialize in writing life and/or accident and health policies.

In addition to its licensing function, DOI is the principal agency involved in the collection of annual taxes paid by the insurance industry. The Department also collects more than 170 different fees levied against insurance producers and companies.

The Department also performs the following functions:

(1) regulates insurance companies for solvency by tri-annually auditing all domestic insurance companies and by selectively participating in the auditing of other companies licensed in California but organized in another state or foreign country;

(2) grants or denies security permits and other types of formal authorizations to applying insurance and title companies;

(3) reviews formally and approves or disapproves tens of thousands of insurance policies and related forms annually as required by statute, principally related to accident and health, workers' compensation, and group life insurance;

(4) establishes rates and rules for workers' compensation insurance;

(5) preapproves rates in certain lines of insurance under Proposition 103, and regulates compliance with the general rating law in others; and

(6) becomes the receiver of an insurance company in financial or other significant difficulties.

The Insurance Code empowers the Commissioner to hold hearings to determine whether brokers or carriers are complying with state law, and to order an insurer to stop doing business within the state. However, the Commissioner may not force an insurer to pay a claim—that power is reserved to the courts.