



REGULATORY AGENCY ACTION

unions from the existing requirements concerning the contents of certain mortgage contracts, deeds of trust, real estate sales contracts, and notes providing for a variable interest rate. This bill is pending in the Assembly Finance and Insurance Committee.

SB 270 (Stirling) would require the Superintendent to report to the Secretary of State the conversion of state-chartered banks into national banking associations, and would provide that the bank shall no longer be considered organized under the laws of California after the report is filed with the Secretary of State. The bill would also require the Secretary of State to file the report with the bank's articles of incorporation. This bill is pending in the Senate Banking and Commerce Committee.

AB 2521 (Johnston) would repeal the entire California Banking Law (California Financial Code sections 99-3904) and replace it with 468 new sections of code. (See CRLR Vol. 9, No. 1 (Winter 1989) pp. 70-71 for further information.) This California Bankers Association-sponsored legislation is pending in the Assembly Finance and Insurance Committee.

DEPARTMENT OF CORPORATIONS

Commissioner: Christine W. Bender
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The Department of Corporations is a part of the cabinet-level Business and Transportation Agency. A Commissioner of Corporations, appointed by the Governor, oversees the Department.

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."

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 Cashiers 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:

OAL Approves Regulation Changes Under the Corporate Securities Law. On February 8, the Office of Administrative Law (OAL) approved the Com-

missioner's proposed changes to sections 260.113 and the addition of new Subarticle 7.2 to Article 4, Subchapter 2, Chapter 3, Title 10 of the California Code of Regulations (CCR), regarding the offering of debt securities by churches. These new regulations became effective on March 10.

The Commissioner also amended section 250.9.1, regarding Department records which are subject to public inspection. Previously, information in the NASAA/NASD Central Registration Depository (other than the names, file numbers, addresses, dates of employment or termination, and the name of employment broker-dealer of California registered securities agents) was exempt from public disclosure; this amendment removes that exemption.

An amendment to section 260.241.4 provides that, effective February 1, 1989, each licensed broker-dealer who is a member of the National Association of Securities Dealers, Inc., shall file changed information contained in its Form BD and Schedules A or B or C and D and E thereto (Uniform Application for Broker-Dealer Registration), through the Central Registration Depository in accordance with its procedures for transmission to the Commissioner.

Also effective February 1, existing section 260.242 was repealed, and new section 260.242 took its place, requiring applications to surrender a certificate as a broker-dealer to be filed on Form BDW (Uniform Request for Broker-Dealer Withdrawal).

Finally, the Commissioner made technical amendments to sections 260.146 (requirement of semi-annual report) and 260.236 (qualifications of investment advisers and associated persons), Chapter 3, Title 10 of the CCR. These amendments became effective on February 9.

Investor Alert Regarding Penny Stock Fraud. On February 3, the Commissioner issued an investor alert regarding high-pressure telephone sales operations touting penny stock offerings. Penny stocks are low-priced stocks traded over the counter, usually by only one or two brokers or market makers.

Investors are receiving unsolicited telephone calls from broker-dealers using high pressure tactics in offering huge profits with "little risk" in penny stock offerings. However, it is easy for brokers to manipulate the price of the stocks and it is difficult for investors to find out if the price is a fair one or if the stock has any value. The Commissioner warned that many of the penny stocks which are being offered to investors are



not legal for sale in this state because they are so speculative and risky.

Enforcement. Peat Marwick Main & Co. has agreed to pay \$9.25 million to settle the state of California's claims and the claims of the class of 12,500 thrift-holders in connection with the April 1984 collapse of Walnut Creek-based Western Community MoneyCenter. The state and the thriftholders sued Peat Marwick for allegedly mishandling the 1982 audit of MoneyCenter. A portion of the settlement funds from Peat Marwick will be used by Thrift Guaranty Corporation to pay off the remaining balance on a state-guaranteed loan. Thrift Guaranty had used the proceeds of that loan in mid-1985 to repay most of the MoneyCenter thriftholder accounts. The remainder of the settlement funds will be used to pay post-takeover interest accrued on those MoneyCenter thrift accounts. (See CRLR Vol. 8, No. 4 (Fall 1988) p. 82 for background information.)

LEGISLATION:

SB 526 (Russell) would increase the time period for filing an application with the Commissioner to qualify any security for which a registration statement has been filed under the Securities Act of 1933. Existing law requires such application to be filed no later than the fifth business day following the filing of the registration statement with the Securities and Exchange Commission; this bill would extend the time period for filing to the twentieth business day. This bill is pending in the Senate Banking and Commerce Committee.

AB 705 (Lancaster) would provide that a certificate to act as a credit union remains in full force and effect until surrendered and accepted by the Commissioner, or until suspended or revoked by the Commissioner. The bill would also require a credit union organized and duly qualified in another state to obtain bond or insurance coverage when operating in California. AB 705 would also authorize the Commissioner, whenever it appears a person has engaged in or is about to engage in any act or practice constituting a violation of the California Credit Union Law or any rule or order thereunder, to bring an action in the superior court to enjoin those acts or practices or to enforce compliance. The bill also sets civil penalties not to exceed \$2,500 for each violation of the California Credit Union Law. This bill is pending in the Assembly Finance and Insurance Committee.

SB 275 (Campbell). Existing law ex-

empts specified securities from qualification with respect to the offer or sale of securities in any nonissuer transaction if the security meets specified criteria and a notice has been filed with the Commissioner setting forth specified information. This bill would eliminate the notice requirement as a condition of this exemption. This bill is pending in the Senate Banking and Commerce Committee.

SB 269 (Stirling) would delete the provision requiring a nonprofit public benefit corporation which changes its status to that of a nonprofit mutual benefit corporation to prepay the minimum tax upon filing the certificate of amendment. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 290 (Greene) would provide that a copy of the latest statement filed pursuant to section 2117 of the Corporations Code by a foreign corporation relating to operations and designating an agent for service of process, and so certified, is sufficient evidence of the appointment of an agent for service of process. When service of process is made against the Secretary of State on behalf of a foreign corporation, this bill would authorize the Secretary of State to notify that corporation of the service by certified mail. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 317 (Stirling) would provide that certain nonprofit corporations organized prior to January 1, 1971, who have never filed an annual statement specifying the address of their principal office in this state, if any, the names and addresses of specified officers, and specified information relating to their agent for service of process will be subject to suspension of their corporate powers, rights, and privileges by the Secretary of State. The bill would also provide that a nonprofit corporation suspended under these provisions may be relieved from suspension upon filing of the annual statement unless the corporation is held in suspension by the Franchise Tax Board. This bill is pending in the Senate Appropriations Committee.

AB 1125 (Chandler) would specify that a director of a nonprofit mutual benefit corporation or cooperative corporation must perform his/her duties in a manner the director believes to be in the best interests of the members of the corporation. This bill would also revise the prerequisites for indemnification of the expenses, judgments, fines, settlements, or other amounts of an agent of a nonprofit or cooperative corporation.

At this writing, this bill is pending in the Assembly Judiciary Committee.

AB 1666 (Wright). Under existing law, specified transactions are exempt from qualification with the Commissioner under the Corporate Securities Law of 1968 if the transaction involves any exchange of securities incident to a merger, consolidation, or sale of corporate assets in consideration of the issuance of securities of another corporation, unless at least 25% of the outstanding shares of any class, any holders of which are to receive securities in exchange, are held by persons who have addresses in this state. This bill would additionally exempt the above transactions where the exchange is in consideration of the issuance of securities of another corporation if, among other things, the exchange of the securities is made with not more than 35 recipient security holders of the acquired corporation, all security holders of the corporation to be acquired have consented to the transaction in writing, each recipient security holder has represented that the acquisition of the securities in the transaction is for the holder's own account and not with a view to or for sale in connection with any distribution of the security, and the offer and sale of the securities is not accomplished by the publication of any advertisement except as specified. This bill is pending in the Assembly Finance and Insurance Committee.

AB 657 (Floyd) would permit the Commissioner to refuse to issue a permit for the qualification of securities in a recapitalization or reorganization unless the Commissioner finds that the proposed plan of recapitalization or reorganization and the proposed issuance of securities are fair, just, and equitable to all security holders affected, and that the proposed plan is in the public interest. This bill is pending in the Assembly Finance and Insurance Committee.

The following is a states update of bills described in detail in CRLR Vol. 9, No. 1 (Winter 1989) at page 72:

AB 10 (Hauser), which would create the California Health Insurance Program, is still pending in the Assembly Finance and Insurance Committee.

AB 27 (Johnston) was amended on April 4 to prohibit life and disability income insurers from requiring an HIV antibody test if the results would be used to determine eligibility for hospital, medical, or surgical insurance coverage or for coverage under a hospital service plan or health care service plan. AB 27 passed the Assembly and is pending in



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the Senate Committee on Health and Human Services.

AB 60 (Isenberg), which would establish the California Catastrophic Health Insurance Program, is pending in the Assembly Ways and Means Committee.

SB 6 (Robbins), which would create the California Health Coverage Association, is pending in the Senate Appropriations Committee.

DEPARTMENT OF INSURANCE

Commissioner: Roxani Gillespie

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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 Codes sections 12919 through 12931 provide for the Commissioner's powers and duties. Authorization for the Insurance Department is found in section 12906 of the 800-page Insurance Code.

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 1,300 insurance companies, which carry premiums of approximately \$26 billion annually. Of these, 650 specialize in writing life and/or accident and health policies.

In addition to its licensing function, the DOI is the principal agency involved in the collection of annual taxes paid by the insurance industry. The Department also collects over 120 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) regulates compliance with the general rating law. Rates generally are not set by the Department, but through open competition under the provisions of Insurance Code sections 1850 *et seq.*; and

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

Through the California Insurance Code, the Commissioner has the power to order a carrier to stop doing business within the state, but does not have the power to force a carrier to pay a claim, a power reserved to the courts. The Commissioner may hold an administrative hearing to determine whether a particular broker or carrier is complying with state law.

The Commissioner is aided by a staff of over 500, located in San Diego, Sacramento, Los Angeles and San Francisco, the Department's headquarters. The Commissioner directs ten functional divisions and bureaus, including the recently reestablished Consumer Affairs Division. This division has been expanded and now includes the Rate Regulation Division. The Consumer Affairs Division is specifically designed to make the DOI accessible to consumers and more accountable to their needs and questions.

The Consumer Service Bureau (CSB) is part of the Consumer Affairs Division and handles daily consumer inquiries. CSB receives over 300 calls each day. Almost 50% of those calls result in the mailing of a complaint form to the consumer. Depending on the nature of the returned complaint, it is then referred to policy services, investigation or CSB.

Since 1979, the Department has maintained the Bureau of Fraudulent Claims, charged with investigation of suspected fraud by claimants. The California insurance industry claims losses of more than \$100 million annually to such claims. Licensees pay an annual fee of \$150 to fund the Bureau's activities.

A Consumer Advisory Panel has been named by the Commissioner as an internal advisor to the Department of Insurance. The panel advises the Department on methods of improving existing services and on the creation of new services. It also assists in the development and distribution of consumer information and educational materials.

MAJOR PROJECTS:

Fireman's Fund Ordered to Stop Cancelling Policies. On January 18, in its first enforcement order under Proposition 103, the DOI ordered the Fireman's Fund insurance group to stop cancelling automobile insurance policies. The company had refused to renew approximately 5,000 auto policies and instead offered only six-month extensions of the policies. Under Proposition 103, companies may only cancel or refuse to renew policies for nonpayment of premiums, fraud, or material increase in the hazard insured against. The Department held a public hearing on January 18, and the administrative law judge hearing the matter recommended a ruling against Fireman's Fund. The Commissioner accepted the ruling, and ordered the insurer to comply with the order. Under the terms of the order, Fireman's was required to cease sending out notices of nonrenewal, rescind any notices it had previously issued, renew all auto policies, and reinstate any insured non-renewed since November 8, 1988. The company indicated that it plans to appeal the decision to the courts.

Travelers Decision Reached. Following a January 7 public hearing (see CRLR Vol. 9, No. 1 (Winter 1989) pp. 73-74 for detailed background information), DOI issued an order requiring Travelers Insurance to renew all of its auto policies cancelled since November 8, 1988, and rescind all the notices of nonrenewal it had issued. DOI Chief Counsel John Faber, who presided at the hearing, had recommended a more lenient course of action, but was overruled by the Commissioner. The Commissioner refused to reveal Faber's original recommendation.

If Travelers violates the final order, it would be liable for fines up to \$10,000 per day per company, to a maximum of \$100,000 per company. The company maintained that the cancellations were part of its plan to withdraw from the California insurance market. Less than ten days after the issuance of the final order, Travelers asked the California Supreme Court to overturn the order. The company has promised to comply with the order during the appeal.

State Farm Settles Over Rating Practices. In November, DOI cited State Farm for rating practices which the Department said unfairly discriminate against new customers. (See CRLR Vol. 9, No. 1 (Winter 1989) p. 74 for background information.) DOI ordered the company to cease its practice of diverting new customers, regardless of the