of such a takeover would be set by negotiation, a court ruling, or the Public Utilities Commission, according to the study. Once the actual price of a municipal takeover could be established by further study, accurate rate projections could be established.

Completed in six weeks, the AOR study has been criticized in the press because the figures supplied to AOR for its projections were provided by SDG&E, and because the report fails to factor in the availability of relatively cheap hydroelectric power if a municipal utility is created.

SENATE OFFICE OF RESEARCH

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Established and directed by the Senate Committee on Rules, the Senate Office of Research (SOR) serves as the bipartisan, strategic research and planning unit for the Senate. SOR produces major policy reports, issue briefs, background information on legislation and, occasionally, sponsors symposia and conferences.

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MAJOR PROJECTS:

Report on the State's Regulation of Financial Institutions (February 1989). Produced by the Senate Advisory Commission on Cost Control in State Government (Advisory Commission) and submitted to the Senate Rules Committee pursuant to SR 40 (Roberti, 1984), this report is the third in a series of studies undertaken to find ways to "increase efficiency, reduce costs, enhance administrative accountability and control, and apply improved program management techniques and systems to state operations."

The substantial deregulation of the financial services industry over the past decade has invited abuse and mismanagement. Changes in the financial services business have increased the competitive pressure on banks and savings and loan institutions (S&Ls).

An unprecedented number of banks and S&Ls have failed over the past five years. Even if not outright failing, 37% of the state-chartered banks were in less than satisfactory financial condition and approximately 17% were in serious trouble in March 1988. Fraud was a factor in approximately 33% of all bank failures. Of the state-chartered S&Ls, 42% were found to be "problem[s]" upon examination by the Department of Savings and Loan (DSL) during fiscal year 1986-87. During that same period, 30% of all national failures of S&Ls occurred in California alone. Fraud was a factor in at least 80% of all S&L insolvencies between January 1984 and June 1987. The flood of institutional failures has engendered monumental problems for both the industry and the federal insurance funds.

Because of the potential for instability in our financial system and the need to minimize the resulting adverse effects on California, the Advisory Commission concluded that the state must undertake "an aggressive reform program aimed at strengthening the supervisory abilities of our financial regulatory agencies"—that is, the Department of Banking and the DSL.

The Department of Banking supervised 389 institutions and $265 billion in assets in February 1988. The DSL supervised 137 state-chartered S&Ls and $147.9 billion in assets in December 1987. The Banking Department recently adopted a "Strategic Plan '88" with "a sound set of goals" for meeting its regulatory objectives; the DSL has no such overall strategy for its regulatory program. In fact, the Advisory Commission found that, in light of the industry's problems, the DSL "had to operate under some significant fiscal and operational constraints," including an inadequate number of examiners.

The profound changes that have taken place in the industry have made state supervision of its financial institutions more important and more difficult. As a result, the Advisory Commission believes that an evaluation of the powers of banks and S&Ls must be made. Then, based on the interests of California citizens and not industry preferences, the legislature must decide whether the present laws should be changed.

The Advisory Commission made the following recommendations:

(1) With regard to both departments:

-the legislature and the departments must reevaluate the departments' existing resources and ensure that they are adequate to supervise their respective licensees;

-the legislature and the departments must create deterrents to and focus greater staff resources (including special fraud units) on fraud and misconduct, which are responsible for so many institutional failures;

-the departments must examine all licensee institutions at least once per year and "troubled" institutions every six months;

-the departments must conduct a thorough review of their information sources and negotiate greater access to federal sources;

-the legislature and the departments must provide salaries and benefits to examiners and supervisory staff comparable to private sector equivalents; and

-the departments should overhaul their human resources objectives by fully implementing Department of Personnel Administration (DPA) recommendations regarding improvement of examiner salaries and benefits; requesting additional authority from the DPA for filling and reclassifying certain examiner classes; and reassessing whether their career counseling programs are meeting the needs of their employees.

(2) With regard to the Department of Banking:

-the legislature should reinstate the $100,000 appropriation cut from the 1988-89 budget to increase examiner training.

(3) With regard to the Department of Savings and Loan:

-the legislature should revise the Department's funding mechanism (currently, assessments from the S&Ls it regulates) by considering larger assessments; funding from the general fund instead; supplementing assessment proceeds by funds from the general fund; or funding through some other methods such as franchise tax offsets;

-the legislature should shield the DSL Commissioner from political pressures by changing the office from a pleasure appointment to a term appointment removable only for serious cause;

-the DSL must develop an operational strategy analogous to the Banking Department's "Strategic Plan '88"; and

-the DSL should conduct joint examinations with the Federal Home Loan Bank of San Francisco where it focuses on operating areas unique to California institutions.

The Advisory Commission also recommended against the consolidation of the two departments into a single "Department of Financial Institutions" because of the substantial differences between the two regulatory structures and the experiences of sister states.