SCOMM

#18:3

Public Control of Public Money

Should States and Cities Have Their Own Banks?

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CONFERENCE/ Alternative State and Local Public Policies

INSTITUTE for POLICY STUDIES
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A modern five-story building sits prominently on a corner of Main Street in downtown Bismarck, North Dakota. A wagon wheel gracing one side of the building accents the logo, "Bank of North Dakota." In all respects save one the bank is quite ordinary. The exception is that the bank is owned by the state of North Dakota. Controlled by a three-person commission, it is the only bank in the United States completely owned by a state government.

The Bank of North Dakota is an historical anomaly, born of the uprisings of Great Plains populism in the early years of this century. It is also a useful model for the future. The bank's assets amount to nearly $400 million, making it the biggest bank in the northern plains states. Some 75 percent of its deposits come from the state government, but it also holds 4,000 business and individual accounts. The Bank of North Dakota employs 83 people. In 1975, it returned $9.2 million ("hugh profits," said a New York Times report).

Last year, Forbes magazine, in a report titled "Living with Sin and Liking It: North Dakota, a Conservative State is Deep into Socialism," noted that the bank was popular even with many Republicans, and though they are ideologically opposed to the state being in the banking business, they appreciate what the bank contributes to the state's economy.

The bank was the product of a hardfought political battle. In 1915, an unsuccessful farmer named Arthur C. Townley--in what one historian described as a "curious blend of socialism and high-pressure salesmanship"--organized North Dakota's Non-Partisan League. The very next year, the League nominated a full slate of candidates and won every statewide elective office but one. League supporters gained an 85 percent majority in the house but failed to control the senate.

Three years later, the North Dakota legislature finally passed the League's "industrial program" in its entirety. Among the program's main provisions was the creation of the Bank of North Dakota, which opened for business on July 28, 1919.

In setting up the bank, the state had issued $2 million worth of bonds to provide its capital. Business interests promptly organized a nationwide boycott of the bonds--the bank had been denounced as "socialistic"--and thereby delayed its operation for several months. Finally, the Chicago Federation of Labor and the Minneapolis Trades and Council Assembly voted to deposit their funds with the Bank of North Dakota. Other union organizations and sympathetic individuals bought the bonds, and the bank got rolling.

Deposits (including mandatory deposits by school districts and other governmental units) amounted to $13 million by January, 1920 and $25 million by the following March. By May 15, 1920 the bank had issued more than $2 million in loans at an interest rate of 6 percent--two-and-a-half percentage points less than its customers had been paying commercial banks. It also had financed a home building association and a new state grain mill and elevator. And it had lent money to counties for seeds and feed for farmers suffering from drought losses.

In 1921, in the midst of bitter internal strife among the Non-Partisan League's top leadership, opponents of the League presented voters with an initiative calling for the bank's dissolution. But the voters defeated the resolution, and their support paid off--in the 1920's and 1930's the bank (according to the New York Times) "rescued thousands of farmers from financial ruin."

Today, the bank does a good business in GI, FHA, Farmers Housing Administration, and Small Business Administration loans, and in federally insured student loans. It also lends money to government agencies and municipalities. Though it is now prohibited from making direct private or commercial loans, it does accept savings and checking accounts (currently numbering about 4,000) from individuals and corporations. Since its founding in 1919, it has returned some $83 million in profit to the state treasury. "That's not bad," says bank president H. L. Thorndal, "on a $2 million investment made 56 years ago."

The other 49 state governments don't own banks, but they do have a good deal to do with banking.[1] State commissions are responsible for regulating banks and savings and loans that do not have federal charters

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[1]The state of Delaware does own stock in a private bank, Farmers Bank of Delaware, but not a majority and exercises little control over the bank's policies. The bank is currently in financial difficulties and requesting bailout funds from the state.

(about two-thirds of the total). State treasuries depend on banks both to handle state funds and to broker state bonds. Bank loan and investment policies at times become political issues and generate political responses. The Illinois state treasury, for example, pursues a "linked deposit" plan, in which state deposits are placed in one or another bank depending on how well the banks live up to various social criteria (such as making mortgage money available without "redlining"). The new Treasurer of Colorado, Sam Brown, has initiated a similar plan in his state.

However, the economic downturn of recent years has led some states and cities to consider more direct involvement in banking. The Massachusetts legislature early this year created a "development bank," the Massachusetts Community Development Finance Corporation, to invest in fledgling enterprises in low-income areas. State-owned commercial banks like North Dakota's are being discussed by legislators in Washington, Oregon, Colorado, New Jersey, Massachusetts, New York, California, and Florida. The cities of Austin and the District of Columbia are studying the feasibility of creating city-owned banking institutions.

OBJECTIVES OF A PUBLIC BANK

The notion of public banks is a step beyond traditional welfare state programs. The basic thrust is to substitute public for private criteria in the investment of money--to broaden the considerations in the placement of funds to include social costs and benefits.

There are at least three general objectives that a publicly owned commercial bank can fruitfully pursue. One is profit. Part of a public bank's portfolio could include commercial and personal loans of the sort any bank might issue. If the state bank is the sole repository of government funds, it is guaranteed a large base of deposits from which to make these loans (and for which it does not have to advertise). Its average return on conventional, "safe" loans may therefore be slightly higher than that of private banks.

Second, public banks can lend money to "high risk" people or enterprises that commercial banks currently won't touch, provided the loans can be justified on other grounds such as reducing unemployment or promoting long term economic development. Applicants in this category might include cooperatives--both consumer and producer--; businesses in high unemployment areas; community-development corporations; and homeowners in low-income neighborhoods. Inevitably, loans in these categories would sometimes entail considerably higher risk than most loans accepted by commerical banks and savings and loans. Rates of return might often be lower than commercial banks would find acceptable, and in some cases the public bank might lose money.

If the public bank did lose money, the risky borrowers in effect would be getting a subsidy, either from the other borrowers (who had to pay higher rates) or from the state or city treasury (which would get lower "profits"). Such an arrangement is not far from standard banking practice. Private banks too have to absorb losses from defaulted loans and bad investments, and they set their rates high enough to cover these losses. The difference is that a public bank could take its losses gambling on a dozen community development corporations with not all succeeding, rather than, say on financing highrise office buildings or luxury condominiums that might be more than the market will bear. If the public bank did this part of its job well, its overall profit might be a few percentage points lower than a private bank's--but other social objectives such as stimulating employment, would be well served.

Finally, a public bank could watch out for consumers' interests by serving as a "yardstick" for bank behavior. Consumer complaints against commercial banks are numerous. Interest rates on loans are frequently hard to ascertain, despite the various truth-in-lending laws. Banks discriminate by race, sex, and marital status in ways that are hard to prove. They "redline" not only certain neighborhoods, but also certain classes of people (the young and the elderly, for example). They engage in accounting practices--the 360 day year, for example, and various ways of calculating interest--that end up costing their customers more than is apparent.

Presumably all these practices increase bank profits, and doing away with all of them might be costly. But a public bank, because people will perceive it as a public institution will be under strong pressure to abolish such practices. And it may well be that helping customers rather than trying to fool them or fleece them will make up the difference in increased business. A "pro-consumer" approach should make private banks spruce up their own practices, if only to "meet the competition."

A public bank should not pursue any one of these objectives--profit, socially useful loan policies, and consumer-mindedness--to the exclusion of the others. Neither can it pursue all at once with equal fervor: compromises and trade-offs will be necessary. But setting up an institution capable of implementing all three gives the state government an immense advantage over conventional approaches to banking regulation. Each specific objective could be pursued alone through the traditional means like taxes and regulations. But regulations by themselves are usually coopted, taxes meet with resistance, and private banking interests too often control the agencies who ought to be overseeing them. A public bank would be a working example that banks do not have to operate as they do and it would go far toward making government the equal rather than the handmaiden of the private sector. Above all, the creation of public banks in cities and states around the country would signify that matters of credit and investment should be open to public debate and decision.

MAKING A CASE FOR A PUBLIC BANK

As evidenced by the circumstances that produced the Bank of North Dakota, actual passage of public bank legislation in a state legislature or a city council will involve a political fight. It is not enough to cite the Bank of North Dakota or the general case for a public bank outlined above. Opponents of public banks will argue that North Dakota was a special case--a rural state cut off from normal credit sources--and that, in any event, the private banking system works fine: it provides the most sensible allocation of credit according to the worthiness of respective borrowers. Any other system is a boondoggle and a government giveaway.

Advocates of public banking have to compile detailed information on the functioning of the existing private system, particularly specific examples of economic behavior that may be profitable to private banks but is socially harmful to the state or city. Taxpayers have to come up with the money to repair the "external costs" of this private behavior.

Major areas to look at include:

<u>Concentration</u>

In most cities, three or four banks hold two-thirds or more of all deposits. In smaller cities, two banks hold three-fourths of all deposits. Overall concentration in banking is about twice as high as in manufacturing. In California, for example, five banks--Security Pacific, Bank of America, Wells Fargo, Crocker Bank, and United California Bank--together control three-fourths of all bank deposits, assets, and offices in the state.

Usually, the largest banks are the greatest political donors to campaigns and finance the most powerful lobbies in the state capitol. These contributions can be compiled from public records. The profit records of these banks can be obtained from local business pages and from annual reports. As the Los Angeles Times reported in mid-1975, "In the midst of America's worst recession since the 1930's, the U.S. Banking industry has just completed its most profitable first quarter in history."

<u>Urban Disinvestment</u>

Also known as "redlining," this is the policy of lending institutions to avoid investing in home mortgages, construction or rehabilitation, and in some cases small businesses in certain urban areas they decide are "undesirable" or likely soon to become "undersirable." An increasing number of studies around the country have documented the existence of "redlining" and related it directly to factors of race, age of housing stock, and income.

In Los Angeles, for example, the Center for New Corporate Priorities, a public interest research group, used a computer to analyze the location and amount of loans by state-chartered savings and loans over a six month period. The results were displayed on a map, colored various shades of red and green to indicate which areas of the county received loans and which did not. The Center's graphic report helped to touch off a debate among state and city officials about "redlining."

In addition to such studies, public hearings on "redlining" can elicit testimony from individuals who have personally suffered from loan denial and from community groups who are trying to save their neighborhoods from the self-fulfilling prophecy of the banks that the area is going downhill.

Strip Mining of Capital

Private banks and savings and loans often seek and accept deposits from low-income, depressed areas, then take the money out of the community for loans elsewhere, much as a multinational corporation extracts profits from an underdeveloped country. Hearings on the proposed state bank bill in New York produced testimony that money is striped from rural communities in upstate New York and funneled into the large banks in New York City, which use it for overseas investments.

The large banks in a state should be required by legislation and in public hearings to provide data on the relationship between the location of deposits and loans within the state.

Community Economic Development

Private banks rarely supply funds to community development corporations. Examples can be gathered, through hearings and letters, of CDC's that have sought bank loans for projects and been rejected.

Small Business

In many states, small businesses, particularly those run by women and minorities, have trouble getting loans. It is easier and more profitable for banks to make large loans to their largest customers. In California, the staff of the state Senate's Committee on Small Business has compiled a file of complaints from small businesses around the state about their troubles in obtaining loan funds.

Cooperatives

Cooperatively-owned enterprises such as supermarkets, drug stores, health centers, etc., have trouble getting loans from private banks. This appears to be based more on ideological hostility on the part of bankers than on the actual prospects of the businesses. Case examples can be collected from coops and from groups trying to start coops on their experience in obtaining money from private banks.

Unemployment

The loan activites of private banks contribute to unemployment in the inner city, rural areas, and certain sectors of the economy. Refusing to to loan money puts people out of work. In addition, making certain kinds of loans also puts people out of work. In California, the Bank of America has readily supplied funds to agribusiness and large farmers to mechanize their operations, thereby throwing farm laborers out of work. At the same time, the bank is not forthcoming with loans to small family farmers or farmworker coops which are trying to find capital to enable them to purchase their own farm land.

In urban areas, banks favor loans to large corporations for investment in capital-intensive activities. Medium-sized companies in California producing solar energy equipment--a relatively labor-intensive business--say that the banks will not finance them.

Often, case examples can be found of large-scale investment by banks in foreign countries. These investments are frequently open to criticism, depending on the country involved and the nature of investment. The Bank of America and Chase Manhattan, for example, had branches in Saigon during the Vietnam War and strongly supported government policies in that region.

Government Bond Market

State and local governments rely on private banks to sell their notes and bonds. Recently, the bond market has been eroded by events in New York City. In Massachusetts, government agencies have experienced refusals to buy their bonds.

A careful study should be made of a state's bond situation and of the responsiveness of private banks to the plight of individual cities.

Environmental Protection

Private banks rarely, if ever, take into account the environmental effects of the loans they make. If a development destroys a shore area or if a new factory pollutes a lake, it is no concern to the bankers who financed the venture. A recent survey by the Center for New Corporate Priorities in Los Angeles found that environmental effects of loans play little role in bank investment decisions.

A survey can be taken of private banks regarding their environmental policies.

Consumer Treatment

Consumer groups in some states, for example San Francisco Consumer Action, have published comparative ratings of banking services in particular cities. Such studies are useful in illustrating the varying quality of consumer services provided by banks and highlighting those areas in which banks are engaged in either misleading or shoddy practices.

STRUCTURE AND OPERATION OF A PUBLIC BANK

The courts have upheld the right of government at all levels to engage directly in business activity. Legal challenges to the Bank of North Dakota and later to the Tennessee Valley Authority were decided in favor of the government. The actual scope of action of state and city governments with regard to public ownership and operation of enterprises such as banks varies considerably from state to state, depending upon whether the state's constituion limits, encourages, or takes no position on such action.

A state's constitution may limit state participation in ownership or operation of enterprise by, for example, prohibiting the state from contracting debts for public works such as railroads, highways, and dams (e.g. Kansas, Minnesota); from loaning its credit in aid of any individual, association or corporation (e.g. Arkansas, Florida, Idaho, Iowa, Minnesota, Nebraska); or from becoming a stockholder in any private corporation (e.g. Iowa). Such limitations are an expression of public policy, not a constitutional principle.

To create the Bank of North Dakota, the state constitution had to be amended to read:

> That the state or any county...may establish and maintain a system of rural credits and thereby loan money and extend credit to the people of this state upon real estate security in such manner and upon such terms and conditions as may be prescribed by general law.

Some of the state bank bills currently proposed, for example, in Washington, require constitutional amendments. In 1932, Justice Brandeis (in New State Ice Co. v. Liebmann) put forward the now generally accepted opinion that a state may "serve as a laboratory; and try novel social and economic experiments..." Over the years, North Dakota has shown that a state government can successfully run a bank. It is no longer a novel experiment.

Municipal governments are creations of state government and exercise such powers as the state delegates to them. Consequently, the range of options available to municipalities in public ownership is potentially as wide as that of the state in which the city is located. City ownership of banks is quite common, for example, in West Germany. There is no reason why a medium-sized city in the United States could not establish its own public bank.

In the drafting of public bank legislation, public accountability and participation should be built into the structure of the bank. This is important because public enterprises can be managed just as autocratically and unresponsively as private enterprises. The Bank of North Dakota, for example, is governed by a three-person Industrial Commission, made up of the governor, the attorney general and that state treasurer. Its activities are watchdogged by a legislative committee and its profits must be returned to the state treasury. This is not the ideal model. As is spelt out in detail in the model legislation in the appendix, it seems preferable to have a board of directors with representatives of labor, consumers, cooperatives, and small business, as well as state executive officers such as the state treasurer.

It is also proposed in the model legislation that branch banks (in states that allow branch banking) have community loan advisory committees to periodically review the activities of the state bank in the community and to recommend certain categories of loans and approaches to economic activity in the community.

As do private commercial banks, the public bank should have speciality officers and desks. For example, the bank might have a department geared to the assistance of the formation of cooperatives. This department would not only evaluate loan applications from existing coops; it would provide technical assistance to fledgling coops around the state or city. A state bank might, like some international development banks, have a rural desk or an agricultural loan department to work with family farmers and with farmworkers wanting to start agricultural coops. There might also be special desks to handle the financial problems of community development corporations.

The public bank, through its research department, would serve an entrepreneurial function by studying possible new markets for the state's products and pointing out new directions for small businesses, coops, and CDC's. The bank's research would also be a valuable guide to the legislature in assessing the overall economic health of the state.

In the initial staffing of the bank, it will be necessary to search out publicly minded individuals from the private banking community. Some experts might be located from existing international development banks. Eventually, the public bank can work with business schools at universities within the state to develop new curriculum for the training of public bankers. Special training programs can be created in public enterprise, management of cooperatives, community-based economic development, and other subjects now neglected by existing, corporate-oriented business schools.

Finally, in states where there exist strong credit unions, they can be joined into the statewide public banking network. In British Columbia, which has a strong history of credit unions, this was done when the publicly owned British Columbia Savings and Trust was established last year. A similar proposal has been made by Bill Batko in his paper outlining a municipal banking system for the District of Columbia.[2]

In its daily operations, the public bank would also provide public education on money and credit issues by producing low-cost, easy-to-read pamphlets on loan options, family budgeting, and how to start small businesses, coops, and CDC's.

Small, community-based private banks are often more responsive to local needs than branches of large multinational banks. The public bank may well find it advantageous to work closely with the smaller banks in the state, joining with them in loan packages aimed at developing the local economy in which the private banks are located.

FINANCING THE BANK

Initial capitalization of the public bank should be by direct legislative appropriation. Initial deposits would include some or all of the state and/or municipal funds now deposited in private banks. This public money need not be removed all at once, but semi-gradually over a period of time. Discretion in this matter should be left to the officers of the public bank.

The bank would solicit demand and time deposits from consumers and private businesses and from socially-minded institutional investors such as churches, universities, and labor unions. The bank would also issue its own bonds and notes.

Public employee pension fund systems at the city, county, and state level could be required to invest a percentage of their assets in the

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[2]Batko's paper is reprinted in the Public Policy Reader prepared for the 1976 Conference held in Austin, Texas

state bank. A detailed study of the California public pension fund system made by Ed Kirshner under contract to the state Department of Employment Development recommends just such a course of action.[3]

UCLA political scientist Karen Orren has proposed a similar requirement for the insurance industry. In her pioneering study, Corporate Power & Social Change: The Politics of the Life Insurance Industry (Johns Hopkins University Press, 1974), Ms. Orren suggests that life insurance companies be required by law to place one third of their investible funds--over seventeen billion dollars nationwide in 1970--in a development bank. She points out that "life insurance funds are well suited to such a plan... (they) carry a fixed rate of interest assumed for the entire period of the insured's 'deposit,' providing a convenient method for setting the interest rate at which the development bank would pay the life company for the use of its money."

In addition to making such a legal requirement for insurance companies regulated by the state insurance commissioner, state's might also consider establishing their own public insurance companies. Three Canadian provinces operate auto insurance companies, investing the premiums to benefit the local economy.[4]

POLITICS OF WINNING

Establishment of public banks, given the predictable resistance of private sector interests, necessitates a comprehensive political strategy.

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[3]The Kirshner study is reprinted in the Austin Conference Public Policy Reader

[4]For more information on public insurance companies, see Case, Goldberg and Shearer, "State Business," Working Papers, spring, 1976

Two elements of that strategy have already been discussed: an assessment of the potential benefits to citizens from the operation of a public bank and an accounting of the social costs eminating from the existing private banking system. One final factor, perhaps the most vital, remains. This is the ideological argument: the contest against the attitude that government can't do anything to improve the quality of life in the U.S.

The Wall Street Journal, for example, argued in an editorial against the New York state bank bill that government is incompetent and incapable of handling business enterprise. The Journal wrote:

"New York City's financial situation may not yet be rotten to the core, but the proposal by the Big Apple's legislative delegation to establish a network of state banks amounts to offering to do for the rest of the state what they have done for Fun City."

In a similar vein, an official in the Massachusetts state government told a Boston Phoenix reporter,

"Bankers are not the brightest group I ever met, but compared to the guys the legislature would put on a state bank board, they're geniuses. You need a certain amount of honesty in government before you can have good public institutions."

One answer, of course, is that we need honesty throughout the society, in private institutions as well as in government. The behavior of the leaders of large corporations is no study in honesty nor ethics. Regarding the issue of government itself, it is not a matter of more or less government--but of what kind of government and for whom? Reforms such as public banks will only be successful if they are related to citizens' movements to put new kinds of political people into office: rank-and-file union leaders, community organizers, environmentalists, womens' activists, senior citizen leaders, etc.

Of course, public banks can be boondoggles and bailouts for private interests--what Ralph Nader calls "lemon socialism"--if they are run by the same old politicians who are beholden to the large corporations for their offices. Partly this can be avoided by building participation and accountability into the structure of the public bank--but only partly. The real answer is to make politics relevant to people's daily lives, so that they do not allow public institutions to be captured by the very forces which necessitate change in the first place.

APPENDIX

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General Books on Banking

THE BANKING SYSTEM: A PREFACE TO PUBLIC INTEREST ANALYSIS by Stanley W. Black III, Glen Canner and Robert G. King, The Public Interest Economics Center, 1714 Mass Ave., N.W., Washington, D.C. 20036, 1975

THE DOLLAR BARONS by Christopher Elias, MacMillan, 1973

CITIBANK, by David Leinsdorf and Donald Etra, A Nader study group report, Viking, 1973

THE BANKERS, by Martin Mayer, Ballantine, 1974

THE CONSUMER'S GUIDE TO BANKS, by Gordon L. Weil, Stein & Day, 1975

Redlining

URBAN DISINVESTMENT: NEW IMPLICATIONS FOR COMMUNITY ORGANIZATION RESEARCH AND PUBLIC POLICY, by Arthur J. Naparstek and Gale Cincotta, National Center for Urban Ethnic Affairs, 4408 8th St., N.E. Washington, D.C. 20017

REDLINING HANDBOOK, Movement for Economic Justice, 1609 Connecticut Ave., N.W., Washington, D.C. 20009

WHERE THE MONEY IS, Center for New Corporate Priorities, 1516 Westwood Blvd., Los Angeles, CA 90024

Bank of North Dakota

"Living with Sin and Liking It: North Dakota, a Conservative State is Deep into Socialism," Forbes, January 15, 1976

"Hard-Nosed Socialism: The Bank of North Dakota Knows How to Make a Buck," Barron's, June 2, 1975

The Bank of North Dakota (Main Street, Bismarck, N.D. 58501) will provide a summary of the bank's history and copy of the bill stablishing the bank upon request.

Public Banking

"State Business," by John Case, Leonard Goldberg, and Derek Shearer, Working Papers, spring 1976

TWO MODELS OF FOREIGN DEVELOPMENT BANKS, by Mya Maung, Center for Community Economic Development, 1878 Mass Ave., Cambridge, Mass. 02140

STATUS OF PUBLIC BANK LEGISLATION

California

In 1975, consultants for the state Department of Employment Development produced a draft state bank bill. A copy of that bill is included in this appendix.

This year, Senators Nicholas C. Petris (D-Oakland) and John F. Dunlap (D-Napa) requested the State Senate to conduct an 18-month feasibility study of a state bank. For up-to-date information on the progress of the study write: Jonathan C. Lewis, Legislative Assistant to Senator Petris, State Capitol, Room 3082, Sacramento, CA 95814

Colorado

As yet, no state bank bill has been introduced in the Colorado legislature. Treasurer Sam Brown is interested in the concept, but he is concentrating on a study of the operations of the existing private banking system, under a foundation grant. Copies of Brown's study should be available by the end of the year.

Brown has instituted a system of "linked" deposits for state tax money deposited in private banks. Information on the criteria that Brown is using in his system is available from the Office of the State Treasurer, State Capitol, Denver, Colorado.

District of Colombia

In 1975, an ad hoc committee established by city council member Nadine Winter looked into the possibility of a public bank for Washington, D.C. The ad hoc committee submitted legislation to establish a Commission on the Establishment of a Municipal Bank, but that legislation has not, as yet, gotten out of committee for a council vote. For up-to-date information on the status of the bank proposal for Washington, D.C., contact ad hoc committee member Bill Batko, c/o Institute for Local Self-Reliance, 1717 18th St., Washington, D.C. 20009, (202) 232-4108.

Massachusetts

A full fledged state bank bill has been drafted and introduced into the Massachusetts legislature in the 1976 session by state Senator Chet Atkins. Atkins expects the bill to have preliminary hearings this spring. The extent of support for the bill and the position of Governor Dukakis are unclear as of this writing.

For a copy of the bill, write: Senator Atkins, State House, Boston, Mass. 02133

New York

Greatest progress toward passage of a public bank bill has occured in New York. A bill to create the New York state bank passed the Assembly in 1975, but was killed in committee in the Republican-dominated Senate. The bill was strongly supported by Assembly speaker Stanley Steingut (D-Brooklyn). Hearings on the bill were conducted in late spring by the Assembly Committee on Banking chaired by Assemblyman George Cincott (D-Brooklyn). Among those testifying were Ralph Nader, Eliot Janeway, H.L. Thorndal, President of the Bank of North Dakota, and James Needham, chairman of the New York Stock Exchange.

Because it is a two year session, the bill can be brought up again in 1976. Steingut still is pushing the measure. For copies of the bill and of testimony from the hearings, write to the: Office of the Speaker, New York State Assembly, Albany, New York, 12224

Oregon

In 1975, a state bank bill modeled directly after the state bank of North Dakota was introduced into the legislature by Rep. George Starr (D-Portland). The bill is currently being studied and redrafted to strengthen it. For current information on the proposal, contact: Office of Rep. George Starr, Oregon State Legislature, Salem, Oregon, 97310

Washington

A state bank patterned exactly after legislation creating the Bank of North Dakota was introduced into the Washington legislature in 1975 by Rep. Michael Parker (D-Tacoma). The measure provoked immediate opposition from the Washington State Bankers Association. If passed, the state bank would become the third largest bank in Washington.

Under attack from the state's private bankers, Parker conceded that the bill could be watered down to prevent the state bank from competing for deposits and loans with private banks. Parker, who is running for Congress in 1976, told the American Banker:

"I'm not criticizing the local banking community in any way. What I see the state bank as being able to do is provide them with more options. We were looking for a more acceptable way we could provide employment. If that's through a state bank that can loan money to other banks at a more acceptable rate than they can get it through the Federal Reserve, that may be the way to do it."

Parker sees the state bank as a "kind of mini-Federal Reserve system" that would serve as a bond bank for local issues, provide more funds for student loans, and offer housing funds at lower rates. The bill requires a Constitutional amendment, since the Washington state Constitution prevents the state from setting up such a bank. As a constitutional amendment, the bill requires two-thirds approval of both houses of the legislature.

The bill was introduced for study in 1975 and for action most likely in 1977. Copies of the bill are available from the office of Rep. Michael Parker, State Capitol, Olympia, Washington 98504.

Florida

Rep. Ray C. Knopke has introduced legislation (HB 2410) in the 1976 session to establish a select joint legislative committee to study the feasibility of creating a state-owned bank. Knopke feels that this is the best strategy, given the strength of the banking lobby in Florida and the newness of the issue. For copies of his bill, write: Rep. Ray C. Knopke, 416 House Office Building, Tallahassee, Florida, 32304.

April 21, 1975

BRIEFING MEMORANDA ON THE

PROPOSED NEW YORK STATE PUBLIC BANK

(A.6531 and A.6532)

Attached are three briefing memoranda concerning the proposal to establish a New York State Public Bank. The first of these memoranda sets out specific issues raised by this proposal and offers responses to these issues. The second of the memoranda sketches the precedent for this bank: the Bank of North Dakota. The third of the memoranda briefly traces the history and evolution of banking in the United States.

These memoranda are not meant to be a comprehensive treatment of the issues at hand. Rather, they present background statements to better acquaint the media with the complexity of the proposal at hand.

MEMORANDUM ONE: BRIEFING MEMO ON THE PROPOSED NEW YORK STATE PUBLIC BANK.

ISSUES AND RESPONSES

NEED FOR A PUBLIC BANK

Q: What are the concerns and problems that led to the conceptualization of the public bank?

A: 1. Redlining -- Redlining is a policy of banks in New York and across the country to avoid investing for new home construction and mortgages in "undesirable" communities. The observable phenomenon that many sections of the State of New York, particularly our cities and low income communities, are unable to obtain financing for new home construction and that existing property renovation and rehabilitation are virtually impossible is the result of this bank policy. The pervasive effects of redlining undermine the very financial structure of our cities and low-income communities.

2. Municipal Bond Market -- The erosion of the municipal bond market is the result of another bank policy. The repeal of the Port Authority covenants and the UDC crisis have shaken the confidence of the banks in the municipal bond market. The recent suspension by Standard and Poor's of New York City's "A" rating has further eroded this confidence. As a result, the financing of municipalities has become an increasingly costly burden.

3. Community Development -- The perception by the banking community that community development is not profitable has led to an almost total lack of long-term capital for community development. As a result, neighborhoods have nowhere to turn for funds making community decay all but inevitable. Lack of this kind of funding by the banks represents a severe disservice to the people of the communities from which the banks draw their funds.
4. Venture Capital -- Venture capital is high risk capital for new industrial and commercial enterprises. This flow of money to innovative businesses is essential to keep the state's economy healthy and to provide a base for future job creation. Being basically risk averse, the banking community has shunned these investments resulting in an almost total absence of risk capital in the state.
5. "Strip mining" of Capital -- The disintermediation of monies has resulted in the flow of money from rural areas to small villages, from towns into cities of increasing size, and finally into the major money centers. Ultimately, this money is exported to other states and countries where it

can earn the higher rates of return than are currently available in the state. Increasingly, monies deposited in New York State are being used to finance development elsewhere in this country and abroad. Doubtless, this process will be accelerated by the statewide Branch Banking Law, and in that context, the following direct quote as reported in the Rochester Democrat and Chronicle, April 10, 1975, from Arthur M. Richardson, President and Chief Executive Officer of Security, New York State Corp., an upstate regional bank holding company, is of relevance:

> "To the internation giants like Citibank, Chase Manhattan and others, their upstate banks are like strip mining operations. The raw material, money, is extracted from our local communities to be used anywhere in the world where they can get the best terms regardless of local consequences."

MORE GOVERNMENTAL BUREAUCRACY

Q: Are there alternatives to a state bank in order to accomplish the same purposes? In other words, do we need a new institution and a new governmental bureaucracy?

A. Yes, we do. For perfectly sound reasons having to do with maximizing earnings per share in the case of commercial banks, and the less clear purpose of increasing capital surpluses in the case of savings banks and Savings and Loans, the banking institutions have historically been unable and continue to be unable to deal adequately with the collection of problems referred to previously. It is pointless to berate the FHA for its historic reluctance to insure in urban areas, (leading to the self-fulfilling prophetic results of disinvestment) and it is equally unproductive to criticize banks for preferring to loan under insured and reduced risk circumstances. However, the socially undesirable results of these policies are observed in the geographical distribution of the New York State savings banks' mortgage portfolio as of December 31, 1974. At that time 44.21 percent or $19,115,000,000 of mortgages were in insured VA or FHA mortgages. Conventional one and two family mortgages were only 18.3 percent of the portfolio or $7,797,000,000 worth. Of the total mortgage portfolio of the savings banks, 51.8 percent or $22,396,000,000 worth was in New York State and the balance or 48.2 percent being $20,840,000,000 was in mortgages outside of New York State.

Clearly, the private sector is not serving the needs of the state. A new governmental agency is needed in order to stimulate the private sector to better serve public needs.

YARDSTICK COMPETITION

Q: How will the state bank effect the performance of existing banking institutions?

A: There is at present no adequate yardstick by which the performance of conventional banking institutions can be measured relative to their performance as underwriters and market creators of governmental financing. Experience in North Dakota with the State Bank of North Dakota established in 1919 is valid historic precedent for seeking to establish this yardstick.

A multiplicity of incentive and guarantee insurance programs would not be sufficient to produce an efficient, coordinated system of public purpose federal and state programs. However, through direct competition and indirect support, the state bank can act as a positive influence on the existing banking structure and thereby achieve a healthy level of "yardstick" competition.

MANAGERIAL COMPETENCE

Q: Where would the managerial competence come from to run this large scale enterprise?

A: National examples abound of special purpose financial institutions such as farmers credit programs and other public purpose banking efforts which have been run competently and profitably so that capital structure is owned by the client population although policy continues to be set by the executive and by Congress. Even private lending institutions will privately admit that there is no reason to suppose the state cannot run this effort in a profitable manner. Attracting competent management is not an insurmountable obstacle.

UNIVERSAL PANACEA?

Q: Are you seriously trying to tell us that this bank is going to solve New York State's financial problems and the financial problems of the cities?

A: Of course not. Opponents of the bill will seek to destroy this valuable institution by imputing to it such vast goals and objectives that it must necessarily fall of its own weight. It will of necessity have relatively modest resources with which to operate.

ANOTHER UDC?

Q: Why isn't this just another UDC?

A: 1. Profitability -- The whole operational premise of UDC was that it was a developer and builder of last resort. The public bank would not be exclusively a lender of last resort. The public bank is charged with the responsibility of being profitable.

2. Flexibility -- UDC is entirely limited to the most difficult form of long term financing whereas the public bank has unlimited flexibility to lend both long and short.

3. Cash Flow -- It was never contemplated that the cash flow from UDC projects would be adequate to pay debt service until the projects were, in fact, complete. It should also be remembered that the banks refused to loan to UDC prior to the completion of the projects.

4. Regulation -- The public bank would be subject to the regulation of the banking department whereas UDC was essentially unregulated.

5. Intent -- There is little relationship between a development organization such as UDC and a bank. These organizations were designed for different purposes and there is no reason to suspect that they will be subject to the same pitfalls.

SOURCES OF FUNDS

Q: Where will the money come from?

A: The money will come from a variety of sources including:

1. Capitalization of $50 million of first instance funds;

2. Municipal deposits and state deposits which at year end

1974 totalled $3.4 billion on hand in state chartered commercial banks;

3. It is contemplated that local assistance funds projected to be $6.2 billion for 1975 will be transferred through the state bank producing an average daily deposit in excess of $11.5 million a day;
4. The state bank will solicit time deposits of all varieties including day of deposit to day of withdrawal, time deposits, certificates of deposits and other like debt instruments. Under consideration is the possible exemption from federal, state and local taxation of interest earned on time deposits in the state bank;
5. The state bank will solicit demand deposits;
6. It is contemplated that the state bank will be an eligible recipient of grants both federal and state and other forms of public assistance to pursue its objectives.

UNSOUND AND DESTRUCTIVE COMPETITION

Q: Won't the state bank destroy other commercial and thrift institutions?

A: Not at all. The state bank will work closely with such institutions and will function in some respects like the import-export bank. It could participate in loans with other banks and could administer loan insurance and guaranty programs. It should be remembered that banking as a regulated industry is a protected industry and it is not the purpose of the public bank to limit competition but to increase competition. The combined effect of the bank holding law and the statewide banks banking law are far more significant events relative to decrease of competition than the state bank could ever be.

INSURANCE

Q: What security will the depositors have that their money will be there when they want it?

A: In addition to the moral authority of the State of New York we are exploring whether it is more appropriate to obtain Federal Deposit Insurance or create a State Deposit Insurance as the State Bank of North Dakota did. Either of these alternatives should provide depositors with firm safeguards that their deposits are secure.

MEMORANDUM TWO

"HISTORICAL PRECEDENT -- THE BANK OF NORTH DAKOTA"

HISTORY

-- The Bank of North Dakota opened in 1919.

-- It is owned by the state government, not private stockholders.

-- It sought to save farmers from ruinous falling agricultural prices following World War I. At that time, private bankers were quick to foreclose on property and slow to grant loans. As a result, the state successfully stepped in and saved many farmers from financial ruin.

OPERATIONS

-- It is run like any other bank and as such, seeks sound, profitable investments.

-- Its assets are four times greater than any other bank in the state.

-- According to Forbes magazine (1/15/75), its rate of return on assets is almost twice as great as any of the 100 largest banks in the United States.

-- It does little direct lending and soliciting of deposits. Rather it seeks large corporate and state accounts and acts to participate in loans initiated by other banks.

-- One of its most valuable functions is to act as a primary market for small municipal bond issues.

-- Local governments are obligated to deposit their funds in the Bank.

-- Run by an Industrial Commission consisting of the Governor, the Attorney General, and the Commissioner of Agriculture.

MODEL FOR NEW YORK STATE

-- New York has parallel problems to those for which the North Dakota Bank was established. For example, the issue of redlining and the lack of capital flowing to low income communities is analogous to the problem faced by farmers in North Dakota.

-- In addition, many New York municipalities and state authorities would benefit from the role the North Dakota Bank plays in bolstering the market for municipal and state bond issues.

SUMMARY

-- The Bank of North Dakota proves that a state government can be successful in the banking business.

-- The Bank of North Dakota also proves that social, public interest needs can be met while profits are simultaneously pursued.

-- The Bank of North Dakota provides a positive competitive influence on the banking system to act in the public interest as well as aid to the existing private banking structure by participating in loans by banks.

MEMORANDUM THREE

"BANKING HISTORY"

INTRODUCTION

-- Banking in New York is a complex scheme of commercial banks and trust companies, savings banks, savings and loans, credit unions, state and federal regulatory agencies.

-- This is the result of an historically decentralized banking system with over 13,700 separately incorporated commercial banks.

-- This is an unusual system. Most other nations have a powerful central bank which does not exist in the United States.

EARLY BANKING

-- In 1791, the First Bank of the United States was established. It was jointly owned by the federal government and private investors. Political division in Congress prevented renewal of its charter in 1811 but it did act to establish banking as an industry in the United States.

-- From 1811-1816, private banks proliferated. With little control and regulation, these banks irresponsibly issued notes causing inflation and widespread monetary disorder.

-- In 1816, Congress created the Second Bank of the United States. This bank ran into political trouble with President Andrew Jackson and in 1836, its charter was not renewed.

MODERN BANKING

-- In 1864, Congress approved the National Bank Act which provided for a national currency and federal chartering of banks. It provided the first real regulation and supervision of the banking system. This Act brought order and stability to banking for a while.

-- Despite the stability achieved under the banking act, true banking reform and the beginnings of modern banking began with the Federal Reserve System, established in 1914.

-- In 1935, after the wave of banking failures during the depression, the Federal Deposit Insurance Corporation was established. The FDIC has brought stability and confidence to the banking system.

BANKING REGULATION

-- Banks can either be chartered federally by the U.S. Comptroller of the Currency or by the state through the State Banking Department. Federally chartered banks are regulated by the Comptroller of the Currency and must become members of the Federal Reserve System. State chartered banks are regulated by the State Banking Department and by the Federal Reserve Board if they choose to join the Federal Reserve System.

-- Membership in the Federal Reserve System imposes certain restrictions on banks but also grants them borrowing privileges. State chartered banks that don't join the Federal Reserve System are supervised by FDIC.

-- State chartered savings and loan associations and credit unions are regulated by the State Banking Department. Federally chartered savings and loan associations fall under the supervision of the Federal Home Loan Bank Board.

TYPES OF BANKS

Commercial Banks

-- They are corporations owned by shareholders.

-- They may be federally or state chartered.

-- They may provide the following services:

-- time deposits,

-- checking accounts,

-- bank credit cards,

-- consumer and business loans, and

-- home and corporate mortgages.

Savings Banks

-- In theory they are owned by their depositors. However, actually there are no owners. Operating capital comes from depositors rather than shareholders.

-- Savings banks are permitted by Federal Reserve Board and the FDIC to pay higher interest rates on deposits than commercial banks.

-- Savings bank services include:

-- savings accounts,

-- home mortgages and general real estate financing, and

-- passbook loans and savings banks life insurance.

-- Savings banks cannot offer checking accounts, personal loan services, or bank credit cards.

Savings and Loan Associations

-- They are similar to savings banks and subject to many of the same limitations.

-- Savings and loan associations are owned by depositors similarly to savings banks.

-- There is limitation on savings and loans for investing their assets in home mortgages. Otherwise, they operate the same as savings banks.

Credit Unions

-- These are organized around existing institutions or organizations and are not generally open to the public.

-- Credit union members own the organization and get paid dividends in lieu of interest.

-- Credit unions engage mostly in consumer loans for the benefit of their members.

DRAFT

CALIFORNIA STATE BANK ACT

A Bill to Create a California State Bank

(1) The legislature finds the following: Nearly ten percent of the labor force during the current rescession are unemployed with chronic and persistent underemployment affecting segments of the population such as the young, the unskilled, and even recent college graduates even in good times.

(2) A lack of sufficient stable, satisfying employment opportunities is the most significant underlying cause of poverty, public dependence, and crime.

(3) Our customary methods of dealing with unemployment, bureaucratic programs of public assistance and temporary unemployment compensation, have gorwn ever more costly to the taxpayer but have failed to alleviate the problem of poverty.

(4) It becomes increasingly difficult for the small businessman, the independent retailer, the family farmer, to compete economically with the major corporations while economic instability combined

with direct and indirect government subsidies increase the concentration of ownership and wealth in the major sectors of our economy such as agriculture, retail marketing and manufacturing.

(5) Competition and opportunity in the private sector are waning and the mosaic of independent entrepreneurs and farmers which formed the middle class is eroding. At the same time the low income population is suffering from chronic limited opportunity for upward mobility because of a lack of venture capital for new business development and a lack of job opportunity.

(6) Our financing mechanisms increasingly fund all but the wealthy as consumers rather than as income producers.

(7) A need exists to provide substantial venture capital to stimpulate additional business opportunity and attendant employment opportunity.

(8) A need exists to provide additional sources of capital funds to small businessmen and family farmers to strengthen their capacity to compete with conglomerates and multinationals.

(9) A need exists for community-based enterprise to deal affirmatively with the hard core problems of poverty and unmet public needs. In addition to creating new jobs, a need exists to provide capital for imperiled existing business to preserve jobs.

I

PURPOSES

1. The Purposes of this act are:

a. To mobilize public funds to provide needed sources of venture capital and financial assistance to preserve existing jobs, create new jobs, strengthen small businesses and the family farmer, preserve competition, eliminate poverty, underemployment in disadvantaged segments of the population, create new opportunities for entrepreneurs and community owned and controlled enterprise, assist communities in financing needed services.

b. To augment the existing commercial banking institutions with a public entity established to provide financial services which existing private mechanisms have not undertaken effectively.

c. To provide an alternative to current indirect government assistance programs which have proven costly but have failed in the main to achieve their objectives.

d. To create a depository for public funds and quasi-public funds such as pension funds, dedicated to the public interest.

II

ORGANIZATION

2. State Bank Created. The California State Bank Corporation (hereinafter called "state bank"), is hereby created as a public corporate agency of the State of California. Unless otherwise specified in this chapter, the state bank shall be exempt from the provisions of the California Financial Code pertaining to banks and related financial institutions.

3. Board of Directors. The state bank shall be governed by a board of directors of 16 persons, composed of the following: The State Treasurer, The Secretary of Business and Transportation, The Director of the State Department of Banking, The Director of Employment Development, The Director of Housing and Community Development, The Director of Agriculture, as well as two representatives of each of the following interest groups: organized labor, the cooperative

movement, small business, community development organizations, and two representatives at large, all of whom shall be appointed by the Governor, subject to confirmation by the State Senate. The initial board members appointed by the Governor shall serve for the following terms: 3 for terms of two, 4 for terms of four, and 3 for terms of six years. Successor board members shall serve for terms of six years each. Vacancies in the board shall be filled by appointment of the Governor, subject to confirmation by the Senate to serve for the balance of the unexpired term. The Governor shall designate the chairman of the board from its membership.

a. Quorum. A majority of the membership of the board shall constitute a quorum for the purpose of conducting the business of the state bank. In determining such majority, duly-appointed representatives of the public officials serving on the board shall have all powers of board members, provided that such substitution has been filed with the chairman of the board prior to any meeting attended by the representative.

b. Compensation. Public official board memers shall serve without salary or other compensation. Appointed members shall be entitled to reimbursement for necessary expenses incurred in the performance of official duties and shall receive a per diem not to exeeed $250.00 for each meeting of the board or a duly-constituted subcommittee of the board attended by the member, provided that the aggregate of such per diem compensation to any single member during any fiscal year shall not exceed $7,500.00.

4. <u>General Powers.</u> The state bank shall have the following general powers:

a. To sue and be sued;

b. To make and execute contracts, and all other legal instruments necessary for the reasonable exercise of its powers and functions;

c. To make and amend By-Laws for its organization and management;

d. To acquire, hold, sell, lease or otherwise dispose of personal and real property in furtherance of its purposes;

e. To appoint officers, agents and employees;

f. To borrow money and issue negotiable notes, bonds or other obligations;

g. To accept and hold deposits from any and all public and private sources;

h. To invest funds held in reserve in obligations of the State or the United States government, or obligations, the principal or interest of which are guaranteed by the State or the United States government;

i. To accept gifts, grants, loans or financial or any other aid from any source;

j. To engage the services of private consultants on a contract basis for rendering professional and technical assistance and advice;

k. To establish, own and control subsidiary corporations or departments and through such subsidiary or departments, to buy, hold, maintain, sell, lease or otherwise dispose of real property and invest in securities and otherwise conduct the business of a trust company, provided that such trust company business is conducted in conformity with Finance Code §§1500-1590;

l. To invest in securities subject to the limitations of Finance Code §§773 and 774;

m. To make loans or to guarantee loans, make grants and subsidize interest rates on commercial loans obtained from private banks;

n. To market and service any bonds or other general obligation issued by any county or municipality, public agency, or any public instrumentality;

o. To do any and all things necessary, incidental or convenient to carry out its functions and purposes and to exercise the powers expressly granted in this act.

4. Executive Functions. The principal executive functions authorized by the board of directors shall be carried out by the president.

a. The president shall be appointed by the Governor, subject to confirmation by the State Senate;

b. Unless removed for cause by the board of directors, the president shall serve a term of six years;

c. The board shall also elect vice-presidents, a secretary and a treasurer to perform such duties as are delineated in the By-Laws;

d. The president may appoint such additional staff as he deems necessary and convenient for the conduct of the state bank's business and affairs.

5. Borrowing Power. The state bank shall have the power to issue negotiable bonds and notes in such amounts as the board determines is necessary to carry out its purpose, including, but not limited to,

payment of principal and interest on obligations of the state bank, the establishment of reserves to secure the repayment of principal and interest, the retirement of bonds previously issued by the state bank, and all other expenditures necessary and incidental to the fulfillment of the powers and functions of the state bank.

a. General Obligations. Except for such bonds as are secured by particular revenues as specifically provided, every issue of the notes or bonds of the state bank shall be general obligations of the state bank payable out of any of its revenues or assets.

b. State Not Obligated. Neither the directors nor any person executing the bonds or notes are personally liable on the bonds or notes by reason of their issuance. The state bank is sole obligor and neither the state nor any of its agencies or political subdivisions shall be liable on any of the notes, bonds or obligations of the state bank. The assets of the state bank shall be the sole source of payment of such obligations, and the bonds shall so state on their face. The bonds do not constitute an indebtedness within the meaning of any constitutional or statutory debt limitation applicable to the State.

c. Board Resolution. Notes or bonds shall be authorized by resolution of the board of directors. Such resolution shall provide for the date the bonds should bear, the date of maturity, the interest rate, the denomination and series, the form of the bonds, coupon or registered, any conversion or registration privileges, the rank or priority of such bond, if any, the manner of execution of the bonds, the terms of redemption, and any incidental terms.

d. Sale. The bonds may be sold at public or private sale, at such price or prices as the board shall determine. Advance notice of any sale of bonds shall be published at least once in newspapers having a general circulation in the City and County of San Francisco, the City of Sacramento, the City of Los Angeles, the City of Fresno and the City of San Diego.

e. Covenants. In connection with the issuance of bonds, the directors may enter into any covenants with bondholders deemed by the board to be reasonable and necessary: (1) The board may proscribe a procedure by which the terms of any agreement with bondholders may be amended or abrogated; (2) The directors may provide for the powers and duties of the trustee and the terms and conditions upon which the trustee or the bondholders may enforce any covenant or rights vested in them under the terms of the bonds, subject to the trustee powers described in Paragraph j

f. Attorney General's Certification. The directors shall submit any bonds to the attorney general for an opinion as to their validity. If the bond issuance in its terms is consistent with the authority of the board under this chapter, and if the bonds when delivered and paid for will constitute binding and legal obligations of the state bank, the attorney general shall certify on the back of each bond that it is issued in accordance with the Constitution and State laws.

g. Tax Exemption. All bonds issued by the state bank shall be free and exempt from taxation pursuant to Article XIII, Section 1-3/4 of the California Constitution, except for estate and gift taxes.

h. Agreement with the State. The State does hereby pledge to and agree with the holders of any notes or bonds issued under this act, that the State will not limit or alter the rights hereby vested in the state bank to fulfill the terms of any agreements made with the holders thereof, or in any way impair the rigths and remedies of such holders until such notes or bonds, together with the interest thereon, with interest on any unpaid installments of interest, and all costs, and expenses in connection with any action or proceeding by or on behalf of such holders, are fully met and discharged. The state bank is authorized to include this pledge and agreement of the state in any agreement with the holders of such notes and bonds.

i. Redemption of Bonds. Notwithstanding and in addition to any provisions for the redemption of bonds which may be contained in any contract with the holders of the bonds, the state may, upon furnishing sufficient funds therfor, require the state bank to redeem, prior to maturity, as a whole, any issue of bonds on any interest payment date not less than twenty years after the date of the bonds of such issue at one hundred five per centum of their face value and accrued interest or at such lower redemption price as may be provided in the bonds in case of the redemption thereof as a whole on the redemption date. Notice of such redemption shall be published in newspapers of general circulation in the cities of San Francisco, Los Angeles, Sacramento and San Diego at least twice, the first publication to be at least sixty days before the date of redemption.

j. Remedies of Noteholders and Bondholders.

(1) In the event that the state bank shall default in the payment of principal of or interest on any issue of notes or bonds after the same shall become due, whether at maturity or upon call for redemption, and such defualt shall continue for a period of thirty days, or in the event that the state bank shall fail or refuse to comply with the provisions of this act, or shall default in any agreement made with the holders of any issue of notes or bonds, the holders of twenty-five per cent in aggregate principal amount of the notes or bonds of such issue then outstanding, by instrument or instruments filed with the Secretary of State and the Clerk of the County of Sacramento, may appoint a trustee to represent the holders of such notes or bonds for the purposes herein provided.

(2) Such trustee may, upon written request of the holder of twenty-five per cent in principal amount of such notes or bonds and having first given the state bank thirty days' written notice of intent to enforce noteholders or bondholders rights:

(a) Enforce all rights of the noteholders or bondholders, including the right to require the state bank to collect fees and charges and interest and amortization payments on loans made by it adequate to carry out any agreement as to, or pledge of, such fees and charges and interest and amortization payments on such loans and other properties and to require the state bank to carry out any other agreements with the holders of such notes or bonds and to perform its duties under this act;

(b) Bring suit upon such notes or bonds;

(c) By suit, require the state bank to account as if it were the trustee of an express trust for the holders of such notes or bonds;

(d) By suit, enjoin any acts or things which may be unlawful or in violation of the rights of the holders of such notes or bonds;

(e) Declare all such notes or bonds due and payable, and if all default shall be made good, then, with the consent of the holders of twenty-five per cent .. of the principal amount of such notes or bonds then outstanding, to annul such declaration and its consequences.

(3) Such trustee shall in addition to the foregoing have and possess all of the powers necessary or appropriate for the exercise of any functions specifically set forth herein or incident to the

general representation of bondholders or noteholders in the enforcement and protection of their rights.

(4) Any suit brought by a trustee against the state bank pursuant to this section shall be brought in the Superior Court of Sacramento County, notwithstanding any provision of the Code of Civil Procedure to the contrary.

5. Capital Reserve Requirement. The state bank shall establish and maintain a capital reserve fund. The capital reserve fund shall at all times be equal to the aggregate of annual debt service payments of the state bank for the current or any succeeding calendar year.

a. The annual debt service shall include all interest payable during such calendar year on all bonds of the corporation then outstanding, the principal amount of all bonds of the corporation then outstanding which mature during such calendar year plus the amount of all sinking fund payments payable during such calendar year with respect to all bonds of corporation outstanding;

b. A sinking fund shall be maintained by the state bank equal to the amount necessary to amortize term bonds pursuant to any resolution of the directors authorizing term bonds and providing for a sinking fund.

6, Capital Reserve Fund, A capital reserve fund shall be established and maintained for;

a. Any monies appropriated by the state for the purposes of such fund;

b, Any proceeds of sale of notes or bonds required, by a resolution of the board authorizing the issuance of such bonds, to be placed in such reserve account; and

c, Any other monies which may be made available to the state bank for the purpose of such fund from any other source or sources.

d. Use of Capital Reserve Fund. The monies held in or credited to the capital reserve fund shall be used solely for the payment of the principal of bonds of the corporation secured by such reserve fund as the same mature, sinking fund payments, the purchase of such bonds of the corporation, the payment of interest on such bonds of the corporation, or the payment of any redemption premium required to be paid under the terms of such bonds, when such bonds are redeemed prior to maturity, Monies in such fund shall not be withdrawn therefrom at any time in such amount as would reduce the amount of such fund to less than the capital reserve fund requirement specified in §5 of this chapter, except for the purpose of paying principal and interest on the bonds of the corporation secured by such reserve fund maturing and becoming due and any sinking fund payments and for the payment of which other monies of the corporation are not available.

e. Income of Capital Reserve Fund. Any income or interest earned by, or increment to, the capital reserve fund due to the investment thereof may be transferred to any other fund or account of the state bank to the extent it does not reduce the amount of the capital reserve fund below the capital reserve requirement.

f. Bond Limit. The corporation shall not issue bonds at any time if upon issuance, the amount in the capital reserve fund will be less than the capital reserve requirement, unless the corporation, at the time of issuance of such bonds, shall deposit in such reserve fund from the proceeds of the bonds so to be issued, or otherwise, an amount, which together with the amount then in such reserve fund will be not less than the capital reserve fund requirement.

g. State Supplement to Capital Reserve Fund. In order to further assure the maintenance of the capital reserve fund and the solvency of the state bank, such amounts as are certified by the chairman of the board to the Governor as necessary to restore such reserve fund to an amount equal to the capital reserve fund requirement, shall be paid by the State to the state bank for deposit in the capital reserve fund; provided that such payments shall in any event be limited to a maximum contribution of $8,000,000 in any given fiscal year and that any contribution to the capital reserve fund in excess of that amount will require specific authorization by the legislature. However, any transfer of State funds to the state bank other than the appropriation for the initial capitalization of the state bank, shall constitute an advancement to be repaid if and when and under such conditions of repayment as are deemed by the board of directors to be feasible.

7. Deposit Reserves. The state bank shall maintain additional reserves equal to the following percentages of the aggregate amount of its deposits:

a. 45% of the aggregate of deposits of public monies from state, county, municipal and other public sources;

b. 25% of the aggregate of all other deposits.

c. Computation. The reserves required by this section shall be computed on the basis of average daily net demand deposit balances covering bi-weekly periods

d. Nature of Deposit Reserves.

(1) Thirty percent of all reserves on deposit shall be in the form of United States currency kept in the bank's vault; and

(2) The remainder may be in the form of notes and obligations of the federal government.

8. Lending Authority. The state bank may engage in the following lending activities:

a. Community Development. The bank may assist municipalities, counties and public authorities in financing capital expenditure for public works and community facilities, including but not limited to, facilities for education, health, social welfare, recreation, sanitation, water systems, housing development, public transportation and public utilities, by direct loans, the purchase of obligations, or guarantees of the payment of principal and interest on obligations duly issued by such public entities to finance projects specified in this paragraph or projects not specified but deemed by the board of directors to be consistent with the purposes of the state bank.

b. Community Economic Development. The state bank may make or guarantee loans to;

(1) Consumer or producer-owned cooperative associations; or

(2) Enterprises organized for the purpose of providing additional employment opportunities in a geogrpahical or demogrpahic section of the State deemed by the board of directors to be economically disadvantaged or subject to sustained unemployment; provided that such enterprise is controlled by the community intended to be benefited; or

(3) Enterprises, owned wholly or partly by an agency of the State, municipality, county or other public entity, organized for the specific and primary purpose of stimulating the economy and creating jobs in an economically disadvantged area.

c. Loans to Persons. The state bank may make loans to individuals provided credit is unavailable to the applicant through conventional commercial lending channels and the state bank finds that having reviewed the feasibility of the proposal, there exists a reasonable expectation and ability to repay the principal and interest, and additionally, that the purpose of the loan is consistent with the purposes of the act.

d. Commercial Loans. The state bank shall make loans to small businesses

(1) To provide for expansion of a labor-intensive activity;

(2) To finance a feasible plan of reorganization provided that such funds:

(a) Are not readily available elsewhere; and

(b) Such loan is necessary to protect existing jobs or to provide for additional jobs,

(3) When the management of the business demonstrates reasonable ability and capacity;

(4) Reasonable fiscal projections reflect the ability of the borrower to service the debt over the term of the loan;

(5) For the purposes of this act small business shall be defined as a business entity having sales during the year prior to the year of no more than $2 million in 1975 dollar values, or employing not

more than 150 employees, and having no more than 25% of the cost of goods manufactured or sold produced outside the State of California, exclusive of raw materials;

(6) The aggregate of loans to any single small business, its affiliates, or subsidiaries, shall not exceed $800,000.00 in 1975 dollar equivalents;

(7) No such loan shall be made for a term exceeding ten or less than two years;

(8) No such loan shall provide for interest only payments for more than the initial 18 months;

(9) All such loans shall provide for full amortization of the principal in equal monthly or quarterly payments over the term of the loan;

(10) Interest on such loans shall be no more than 1/2 of 1% over the then current prime commercial lending rate;

(11) All such loans will subject to the further conditions that the borrower will:

(a) Fill an agreed percentage of positions with persons categorized as underemployed by the State Employment Development Department; and

(b) Undertake on the job

training for an agreed upon number of persons categorized as underemployed with the aim of creating for such persons, full time positions;

(c) Establish and implement a suitable affirmative action plan for hiring and upgrading minorities and women;

(d) Implement a program to enable employees to obtain for consideration, an equity interest in the business and a corresponding share of the profits.

(12) The limitations applied on loans by commercial banks enumerated in Financial Code §§1221-1235 shall apply to commercial loans made by the state bank.

9. Subsidiaries or Departments. The state bank shall, within one year after commencement of its operation, establish the following departments:

a. Investments. A trust department for the specific purpose of acquiring, where appropriate, securities to provide venture capital for entities eligible for loans under Paragraph 8 of this act.

b. Land. A land bank department to acquire, maintain and lease land deemed by local and regional public planning entities to be suitable for development for low and moderate-income residential use or deemed suitable for industrial and commercial use in areas in which the board of directors has found a condition of persistent underemployment. Lands so acquired shall be leased on such terms as will provide housing available for purchase or rental at reduced costs attributable to the terms of the lease, and in the case of industrial and commercial land will provide an incentive for the establishment of labor-intensive enterprises in an area of persistent underemployment.

c. Technical and Other Assistance. The bank shall provide technical assistance to eligible borrowers to facilitate sound planning and fiscal management of the enterprise. Technical assistance to non-profit entities may include planning grants and seed money grants comparable to investments in profit-making entities to provide venture capital.

10. Deposits. All public moneys possessed or controlled by the State, any county or local government and any agency or instrumentality of the State, county or a local government, shall be deposited in the state bank.

a. Agents. In any county in which the state bank does not have a branch suitable for a depository, it shall designate an appropriate commercial bank to serve as its local agent. The state bank may enter into agreements with commercial banks to serve as an agent for deposit of public funds on condition that such banks agree to establish policies and a program to affirmatively promote job development in California through its lending and investment practices. Standards governing such agreements shall be prepared and adopted by the board of directors.

b. Public Moneys. By "public moneys" is meant: all revenues from taxes, assessments, income from public services, proceeds from bond sales, grants, revenue sharing funds, and transfers from other public sources including state and federal sources, and any other fund maintained by any public entity whatsoever for any public purpose except that lawful reserves maintained by public entities which are other than in cash deposits, whether or not interest bearing, shall be exempt from these provisions and nothing herein shall be construed as limiting the rights of such entities to maintain such reserves.

11. Offices.

a. Principal. The principal office of the state bank shall be Sacramento.

b. Branches. The state bank shall, as soon as practicable but in no event more than one year following the commencement of operation, open full service branches in the following cities: Los Angeles, San Francisco, Oakland, San Diego, Fresno, Redding, Ukia, Eureka, Stockton, Bakersfield, Santa Maria, Monterey, El Centro, Riverside, and San Bernardino. Other branches may be opened at such times and in such places as are deemed by the directors to be convenient.

12. Advisory Committee. A public advisory committee to the state bank shall be established in each county in the State.

a. Membership. The membership of the advisory committee shall consist of a total of six persons: two each from the business community, organized labor and the general public; and shall be appointed by the board of directors for terms of three years.

b. Functions. The advisory committee shall serve as liason between the staff of the state bank and the community. They shall assist persons and entities seeking to use the state bank's services in developing suitable applications and plans and shall evaluate applications to the bank and make recommendations to the state bank as to the probable effect of the assistance requested on the local economy. Advisory committees shall also particpate with bank officials in negotiating conditions for loans which maximize positive economic benefit to the local economy, particularly the job market.

c. Staff Assistance. An adequate number of bank employees shall be assigned the responsibility of working with advisory committees, State and local agencies and business in order to make the services of the bank readily available and to provide assistance in meeting the requirement for assistance of the state bank. The reasonable cost of providing technical assistance may be charged to recipients.

13. Space. The State General Services administration shall elicit the cooperation of State agencies in making suitable space available to the state bank for the purposes of its branches.

14. Accountability.

a. Examination. Once every three years the Director of the State Department of Banking, in cooperation with the State Treasurer, shall conduct a full examination of the state bank. The examination shall include, but not be limited to, a review of accounts, books, receivable, disbursements, contracts, reserves, funds, investments and any other matters material to its financial standing.

b. Audit. Additionally, the state bank shall annually obtain an independent certified audit of its financial standing.

c. Annual Report. An annual report of the financial condition of the state bank shall be submitted to the Governor and the legislature within 180 days after the end of its fiscal year. The report shall include a detailed statement of operation, including but not limited to, receipts, expenditures, assets, liabilities, laons, financial assistance, reserves, bonds and other obligations of the bank.

d. Public Disclosure. All loans, financial assistance and investments shall be public information, and quarterly reports of the banks' lending and investment activities shall be available to the public for inspection at all branches:

(1) Any and all resolutions of the board as well as any guidlines or interpretations of bank policy utilized generally to carry out the functions

of the bank statewide, shall be available for inspection by the public at any branch;

(2) Requriements for loans and other forms of assistance shall be simply and clearly stated to enable applicants to gain a clear understanding of pertinent requirements;

(3) All meetings of the board of directors shall be open to the public and the minutes of the board including the minutes of the investment committee shall be available for public inspection.

15. Capital. The state bank shall be capitalized with $25 million hereby appropriated for such purpose. An additional $1 million is hereby appropriated for advancement by the State Treasurer to the state bank within ten days of the enactment of this legislation to defray its initial expenses incurred in planning and organization. The $25 million appropriation shall be transferred to the state bank by the State Treasurer from the general funds of the State within ninety days after the enactment of this act or ten days after the initial meeting of the board of directors whichever first occurs.

16. Tax Exempt. The property, real, personal and intangible, and income, shall be exempt from taxation.

17. Inconsistent Provisions. Any provisions of any other law inconsistent with the provisions of this act shall be superceded to the extent of such inconsistency and the provisions of this act shall be controlling.

18. Separability. A determination that any portion of this act is unconstitutional or invalid for any other reason shall not effect the validity of any other portion of the act not specifically invalidated.

19. Urgency Legislation. This act shall be deemed to be urgency legislation necessary for the immediate preservation of public peace, health or safety within the meaning of Article IV of the Constitution and shall take effect immediately on its enactment. The facts constituting such necessity are the high levels of unemployemnt which prevail generally throughout the State and particularly the chronic underemployment which affect certain segments of the population.

The National Conference on Alternative State and Local Public Policies was founded in Madison, Wisconsin, June, 1975. It is a major meeting place and forum for elected and appointed officials, community organizations, political activists and technically trained experts interested in alternative politics and programs at the state and local level. Discussions and workshops within the National Conference include questions of political strategy. However, concentration is on the specific nuts and bolts of programmatic alternatives. Subjects considered include land use, tax reform, consumer protection, agricultural policy, minority employment, public power, community and state-owned enterprises, control of natural resources, women's issues, public employees, and many others.

The National Conference has its headquarters in Washington, D.C., at the Institute for Policy Studies. Besides holding regional and topical conferences, and an annual national conference in June, the national office maintains a Clearing House of Alternative Legislation. The National Conference publishes a quarterly newsletter, an Alternative Legislation Series, and a Public Policy Pamphlet Series. A Public Policy Reader is prepared for the annual national conference and is also available from the national office. Finally, the national office coordinates a series of task forces composed of local officials, planners and informed citizens who are drafting model legislation.

The National Conference was organized to be of service to state and local public officials, as well as others who are interested in alternative programs. Your communications can be of great help in furthering the work and extending the influence of the Conference. Please send information, new names, and suggestions to:

Barbara Bick, National Coordinator
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