2003 SUNSET REVIEW

Colorado Department of Regulatory Agencies
Office of Policy and Research

Division of Banking

October 15, 2003

STATE OF COLORADO

DEPARTMENT OF REGULATORY AGENCIES
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Bill Owens
Governor

October 15, 2003

Members of the Colorado General Assembly
c/o the Office of Legislative Legal Services
State Capitol Building
Denver, Colorado 80203

Dear Members of the General Assembly:

The Colorado Department of Regulatory Agencies has completed its evaluation of the Colorado Division of Banking. I am pleased to submit this written report, which will be the basis for my office's oral testimony before the 2004 legislative committee of reference. The report is submitted pursuant to section 24-34-104(9)(b), of the Colorado Revised Statutes (C.R.S.), which states in part:

> *The department of regulatory agencies shall conduct an analysis of the performance of each division, board or agency or each function scheduled for termination under this section...*
>
> *The department of regulatory agencies shall submit a report and supporting materials to the office of legislative legal services no later than October 15 of the year preceding the date established for termination….*

The report discusses the question of whether there is a need for the regulation provided under Articles 1 through 25 of Title 11, C.R.S. The report also discusses the effectiveness of the Division of Banking in carrying out the intent of the statutes and makes recommendations for statutory and administrative changes in the event this regulatory program is continued by the General Assembly.

Sincerely,

Richard F. O'Donnell

Richard F. O'Donnell
Executive Director

2003 Sunset Review
Colorado Division of Banking

EXECUTIVE SUMMARY

Department of Regulatory Agencies

Bill Owens
Governor

Richard F. O'Donnell
Executive Director

Quick Facts

What is Regulated? State-chartered commercial banks, industrial banks, and trust companies. In 2002, there were 128 regulated institutions in Colorado as follows:

- 114 Commercial Banks
- 4 Industrial Banks
- 10 Trust Companies

Who is Regulated? State-chartered commercial banks, industrial banks, and trust company officers and employees.

How is it Regulated? Division of Banking staff conduct examinations of state-chartered institutions and licensees, and examine the following functions:

- Public Deposit Protection Act compliance;
- Trust departments;
- Electronic funds transfer;
- Electronic data processing; and,
- Uniform Consumer Credit Code compliance.

What Does it Cost? The FY 01-02 budget to oversee this program was $3,316,101. In FY 01-02, there were 38.5 FTE dedicated to the Division.

What Disciplinary Activity is There? During the period FY 97-98 to FY 01-02, the Division's enforcement actions consisted of:

Board Resolutions	11
Memorandum of Understanding	7
Cease and Desist Order	2
Other	2

Where Do I Get the Full Report? The full sunset review can be found on the internet at: www.dora.state.co.us/opr/2003Banking.pdf

Key Recommendations

Continue the Division of Banking until 2013
The Division of Banking (Division) is the state agency that ensures a safe and sound banking industry in Colorado by means of its state bank chartering procedures, bank examinations, enforcement actions, and other regulatory activities. The Division should be continued until 2013 given that by means of its oversight of the banking industry, it serves a fundamental role in maintaining a healthy Colorado economy.

Reduce the size of the Banking Board by one member and alter its composition to make it non-partisan
Partisan politics do not play any part in Board deliberations and actions. The Banking Board is highly professional and deals mostly with technical matters specific to banking. An eight-member board is not consistent with the size of most state boards. We recommend therefore that the statutory provision that the Board be comprised of not more than four members from the same major political party be repealed, and that the size of the Board be reduced to seven members.

Institute an independent appeal process regarding "material supervisory determinations", define this term to include bank examinations, and establish by rule criteria to govern appeals to the Board
The Division does not currently have an independent appeals process in place to satisfy any concerns that state chartered banks might have regarding mandatory state examinations or other supervisory actions. Consequently, enhancing the fairness and effectiveness of this aspect of regulation is important. The fundamental purpose of such an appeals process is to increase the integrity of regulation and to provide an opportunity for correction when an appeal is successful.

Authorize the Bank Commissioner to examine any relevant relationship between state banks, affiliates, and third-parties
It is important to have access to financial information from third-party and affiliate entities that exercise significant control over an insured institution's loan portfolio, particularly when the institution is relying on the service provider to indemnify the bank for any losses in the loan portfolio and to provide information to the bank regarding the status of the portfolio. Without this third-party access, bank examiners cannot accurately determine the insured institution's true financial condition and potential risk to the industry.

…Key Recommendations Continued

Clarify that more than one loan production office is permitted
In May 1995, the General Assembly adopted House Bill 1355 to make conforming amendments to Colorado law in relation to the Riegle-Neal Interstate Banking and Efficiency Act of 1994. This federal law lifted the limitation on the number of permissible bank branches. However, loan production office limitations were not changed at that time in the Colorado Banking Code.

Make the Banking Code consistent with the Financial Institutions Reform, Recovery and Enforcement Act of 1989
The Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989, as amended, subjected the real estate industry and appraisers to increased federal oversight. Under FIRREA either a state-certified or licensed appraiser must be used for all real estate-related transactions of $250,000 or more. Currently Colorado law sets this amount at $100,000. To make Colorado's Banking Code conforming to FIRREA, as well as to account for appreciation in property values, the $250,0000 threshold should be incorporated into Colorado law.

Repeal the Colorado Investment Deposit Act
The administrative burden placed on banks and the Division has increased regulation without meeting the original public policy objectives of the Colorado Investment Deposit Act. Since 1996 only two banks have reported accepting investment deposits, and as of December 31, 2002, the total amount of money involved in the program was approximately $300,000 in the form of outstanding loans. Despite low bank participation, the Division is required to send out annual reminders and forms to all state banks, industrial banks, and national banks.

The Division should create and implement a comprehensive recruitment, selection, retention, training, and retraining strategy to address its bank examiner shortage
One of the most important issues facing the Division of Banking is adequate staffing. Recruiting and retaining qualified staff to operate the examination unit is a continuing challenge according to the Director of Examinations. The examination of banks is the core function of the Division. Due to the specialized nature of the work, bank examiners take approximately three to five years to become fully proficient, especially when an individual has had no prior regulatory experience. Even experienced examination staff require training to stay current with changes in laws and regulations, as well as industry changes that affect the safety and soundness of banks.

Major Contacts Made In Researching the 2003 Sunset Review of the Division of Banking

Federal Reserve Bank of Kansas City-Denver Branch
Federal Deposit Insurance Corporation
Independent Bankers of Colorado
Colorado Bankers Association
1st Bank Holding Company of Colorado
State of Colorado Division of Banking
Banking Board Members

What is a Sunset Review?

A sunset review is a periodic assessment of state boards, programs, and functions to determine whether or not they should be continued by the legislature. Sunset reviews focus on creating the least restrictive form of regulation consistent with the public interest. In formulating recommendations, sunset reviews consider the public's right to consistent, high quality professional or occupational services and the rights of businesses to exist and thrive in a highly competitive market, free from unfair, costly or unnecessary regulation.

Sunset Reviews are Prepared By:
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Background

The Sunset Process

The regulatory functions of the Division of Banking (Division) in accordance with section 11-102-101(3) of Colorado Revised Statutes (C.R.S.), shall terminate on July 1, 2004 unless continued by the General Assembly. During the year prior to this date, it is the duty of the Department of Regulatory Agencies (DORA) to conduct an analysis and evaluation of the Division pursuant to section 24-34-104(9)(b), C.R.S.

The purpose of this review is to determine whether the Division should be continued for the protection of the public and to evaluate the performance of the Banking Board and staff of the Division. During this review, the Division must demonstrate that there is still a need for the regulation of state banks and that the regulation is the least restrictive consistent with the public interest. DORA's findings and recommendations are submitted via this report to the legislative committee of reference of the Colorado General Assembly. Statutory criteria used in sunset reviews may be found in Appendix A.

Methodology

As part of this review, DORA staff attended Banking Board meetings, interviewed Division of Banking staff, reviewed records, interviewed officials of state professional associations, canvassed stakeholders, and reviewed Colorado statutes and rules.

A glossary of banking terms may be found by way of the Internet at americanbanker.com

History of Regulation

State regulation of Colorado banks started in 1877, one year after statehood was achieved, when the Colorado General Assembly first codified the process by which banking associations could be chartered and operated. In addition to setting forth the rudimentary powers and duties of banks and the obligations of bank directors, officers, and stockholders, this initial legislation also required banks to submit semi-annual examination reports to the State Treasurer.

In 1877, banks possessed the latitude under the dual banking system, as they do now, to choose whether they wish to operate under a state or national charter. Colorado's venture into state banking regulation occurred at a time when the federal government was chartering, supervising, and examining all nationally chartered banks through the Office of the Comptroller of the Currency (OCC). Consequently, when Colorado's earliest banks chose to operate under a state charter, they were subject only to supervision and regulation by the state authority.

Two developments in the 1870s and 1880s led to a resurgence in state bank chartering and firmly established state banks as an alternative to national banks. The growing use of checks was the first. Checkable deposits increased rapidly in this period in relation to bank notes as checks became more widely accepted and proved to be safer and more convenient to use in many transactions. The decline in the importance of bank notes served to reduce much of the earnings advantage national banks held over state banks. The second development was a decline in the profits national banks could make on notes.[1]

Just as the federal government verged on expanding its regulatory authority, the Colorado Legislature increased state regulatory authority over state-chartered banks by creating the office of the State Bank Commissioner in 1907. The statutory authority of the Commissioner included the granting of state charters, the examination and investigation of banks, the collection of fees, and the liquidation of insolvent institutions.

The power of the Commissioner to act as the sole state regulator of banks remained undiminished until 1913. At that time the enabling legislation was amended to give the Governor, Attorney General, and State Treasurer power to override the Commissioner's denial of a charter application. In was not until the 1957-58 overhaul of the Banking Code that the Banking Board was established which, together with the Commissioner, operated within the Banking Department as a free-standing agency to oversee and administer the Banking Code. The Division of Banking was subsequently transferred to the DORA in 1968 with the passage of the Administrative Reorganization Act.

Other milestones include the jurisdictional expansion of the Commissioner and the Division to include the trust departments of commercial banks (1907), industrial banks (1923), credit unions (1931), trust companies (1947), money order companies (1959), debt adjusters (1963), and public money depositaries (1975).

Legislation enacted in the period 1988 through 1990 redefined the structure of the Division of Banking and the duties and scope of authority of the Commissioner and the Banking Board. In 1988 oversight of credit unions was transferred to the Division of Financial Services. Beginning in 1989 annual audits became a requirement for banks and trust companies.

In 1992 the Division of Banking became cash funded based on assessments imposed on regulated financial institutions. Legislation in 1993 required state-chartered trust companies to conduct a substantial portion of business in Colorado. In 2003 House Bill 03-1257 recodified the Banking Code. A summary of this legislation may be found below.

[1] Spong, Kenneth. 2000. *Banking Regulation: Its Purposes, Implementation, and Effects* (5th Ed.), p. 19. Kansas City, MO: Federal Reserve Bank of Kansas City.

The Banking System of the United States

According to Kenneth Spong (2000) of the Federal Reserve Bank of Kansas City, the main components of the U.S. banking system are banks, bank holding companies, and financial holding companies. Commercial banks are the largest group of depository institutions in the United States, controlling over three-fourths of all deposits nationwide. Banks were the first type of depository institution in this country and have attained their present position by developing many financial services desired by the public. Throughout much of their history, banks could be distinguished from other financial institutions by the type of charter they were granted and the financial powers accompanying such charters. Even today, state and federal laws typically define banks by their charter and by the services they can offer.

All banks accepting deposits from the public must obtain a national or state bank charter before they can open for business. The first bank charters in the United States were granted by means of special legislative acts. Currently, the chartering process involves a number of well-defined administrative steps. To form a national bank, the organizing group must file an application with the Comptroller of the Currency. The Comptroller then reviews the application and, if all criteria are satisfied, issues a national charter. Similar procedures exist at the state level with state banking commissioners, agencies, or boards granting charters for state banks. The specific criteria examined in the chartering process have evolved over time and vary between state and federal authorities. The basic purpose, however, is to assure that institutions accepting funds from the public are competent and deserving of the public's trust.

Before opening their doors, national banks must obtain federal deposit insurance, and nearly every state has similar requirements for state banks. Banks seeking federal deposit insurance must apply to the Federal Deposit Insurance Corporation (FDIC), and the FDIC must evaluate each request according to a number of statutory factors. In addition, state banks may choose whether to apply for Federal Reserve System membership, while national banks automatically become members once a charter is granted. As a result of these chartering and related decisions, three principal categories of banks exist: national banks, state member banks, and state nonmember banks. Additionally, other types of banks are sometimes listed as part of the banking system. These include uninsured state banks, industrial banks, trust companies, private banks, bankers' banks, and certain savings banks.

Receiving a charter entitles banks to engage in a number of activities, but also prohibits them from exercising other powers. These limitations can vary between national and state charters, and from one state to another. National banks derive their fundamental powers from federal law, while state bank operational requirements are primarily outlined in state statutes. When issues of national policy prevail, however, state banks must follow the relevant federal laws. Similarly, national banks may be subject to state statutes whenever federal law defers to state practices, or when state laws do not place national banks at a disadvantage.[2]

[2] Spong, Kenneth. 2000. *Banking Regulation: Its Purposes, Implementation, and Effects* (5th Ed.), pp. 36-37. Kansas City, MO: Federal Reserve Bank of Kansas City

The supervision and regulation of Colorado state-chartered banks, industrial banks, and certain trust companies are conducted within the framework of the dual banking system. The distinguishing feature of the system in the United States is the ability of banks to make a free choice between state and federal chartering and regulation. The states and the federal government act independently to charter, regulate, and supervise financial institutions. The system has produced a decentralized banking industry characterized by a number of checks and balances. Although the system has been criticized as duplicative, the existence of a parallel regulatory system keeps both halves of the system from becoming unreasonably burdensome or costly. Additionally, a set of checks and balances exists within the regulatory system for state-chartered banks, as both the Division of Banking and the Federal Deposit Insurance Corporation (FDIC) or Federal Reserve regulate and supervise these institutions from different perspectives. The state, as chartering authority, determines what the bank may do and where it may operate. The FDIC, as deposit insurer, examines nonmember banks to protect insured deposits from undue risk. The Federal Reserve, as the central bank, supervises state member banks, but also serves as the lender of last resort and ensures the free flow of funds through the banking system. Table 1 depicts the current regulatory structure of the U.S. banking system.

Table 1
The Present Bank Regulatory Structure of the United States

<table>
<tr><th></th><th rowspan="2">National Banks</th><th colspan="3">State Banks</th></tr>
<tr><th>Members of the Federal Reserve System</th><th>Insured Members</th><th>Uninsured</th></tr>
<tr><td>Chartering Authority</td><td>Comptroller of the Currency</td><td colspan="3">State Banking Department</td></tr>
<tr><td rowspan="2">Supervisory and Examining Authority</td><td rowspan="2">Comptroller of the Currency</td><td colspan="3">State Banking Department</td></tr>
<tr><td>and Federal Reserve System</td><td>and FDIC</td><td></td></tr>
<tr><td>FDIC Insurance</td><td colspan="4">Upon FDIC Approval</td></tr>
<tr><td>Federal Reserve Membership</td><td>Automatic with Charter</td><td>Upon Federal Reserve Approval</td><td></td><td></td></tr>
<tr><td rowspan="2">Approval for Branch Applications</td><td rowspan="2">Comptroller of the Currency</td><td colspan="3">State Banking Department</td></tr>
<tr><td>and Federal Reserve System</td><td>and FDIC</td><td></td></tr>
<tr><td rowspan="2">Approval for Bank Mergers [1, 2]</td><td rowspan="2">Comptroller of the Currency</td><td colspan="3">State Banking Department</td></tr>
<tr><td>and Federal Reserve System</td><td>and FDIC</td><td></td></tr>
<tr><td>Approval of Bank Holding Company Formations and Acquisitions [2, 3]</td><td colspan="4">Federal Reserve System</td></tr>
<tr><td>Financial Holding Company Certification and Prior Notice of New Activities</td><td colspan="4">Federal Reserve System</td></tr>
</table>

[1] If the bank resulting from a merger is insured, the responsible federal agency also requests reports on the competitive effects from the Department of Justice and the other two federal banking agencies. The two banking agencies are not required to file these reports if the merger does not raise competitive issues.

[2] Between the approval and consummation dates of a bank merger or a bank holding company acquisition involving a bank, the Department of Justice may bring action under the antitrust laws.

[3] The Federal Reserve Board is required to notify and solicit the views of the Comptroller of the Currency on proposed holding company acquisitions of national banks and the appropriate state banking department on the proposed acquisition of a state bank. When the Federal Reserve sends the notification letters, a copy is commonly sent to the FDIC. Any uninsured bank becoming a subsidiary of a holding company must obtain federal deposit insurance.

Source: Spong, Kenneth. 2000 *Banking Regulation*, p. 52.

The Dual Banking System in Colorado

The U.S. Congress established by way of the National Bank Act of 1864 the national banking system as a means of achieving the economic policy objectives of the United States, including a stable and reliable national currency, availability of private credit on a national basis, and sound banking services through rigorously supervised banks. Despite Congress' strong preference for national banks, state banking was able to adapt simply by substituting deposit-taking for note-issuing, and by taking advantage of state regulations designed to permit state banks to engage in many activities deemed too risky for national banks. As a result, the dual banking system was born. Reflecting the country's basic ambivalence about banking in general, as well as the use of national power, a less confrontational Congress reconciled itself over time to a dual banking system rather than a unified one, embracing a more benign view of state banking as a legitimate expression of state sovereignty and as source of healthy competition.[3]

Many bank products and services that now seem routine evolved as a result of the regulatory competition fostered by the dual banking system. Innovations like variable rate mortgages, interest-bearing transaction accounts, home equity loans, and even the checking account, first appeared in banks under the supervision of state regulators. Through initiatives of federal regulators, banks have been able to expand securities and mutual fund activities, sell annuities, and certify the security of Internet transactions—all to the benefit of consumers. Allowing banks a choice of a national or state charter forces regulators to update and improve examination techniques and examiner training, lest banks under their jurisdiction opt to change their charter type. Furthermore, regulatory authorities are encouraged to take a more positive posture on financial innovation and healthy risk-taking when there are charter alternatives. Regulatory choice drives down costs and increases the speed with which new products and services are developed and approved.[4]

The main criticism leveled against the dual banking system revolves around questions of inefficiency. The current system has given rise to multiple federal and state banking regulations. The role of federal and state regulators is determined by the type of charter selected, as well as other factors (see Table 1). In areas where federal and state governments have joint authority, regulation is normally undertaken on a shared basis. However, even nationally chartered banks are subject to major policy decisions such as branching, usury, and interstate banking that are delegated to the states. On the other side of the coin, federal regulators have considerable power to regulate state chartered banks, especially when state laws require banks to carry FDIC insurance.

[3] Williams, Julie, L., March 17, 2003. *The OCC, the National Bank Charter, & Current Issues Facing the National Banking System*, pp. 41-42. Washington DC: Financial Services Conference

[4] American Bankers Insurance Association. "The Benefits of Charter Choice: The Dual Banking System as a Case Study", pp. 3-4.

The existing system of banking regulation did not evolve from a centralized plan, but was instead formed by a series of responses to economic emergencies. While most of these responses tightened regulation and centralized authority, some recent legislation has moved in the opposite direction toward deregulation. This trend has raised important questions about the allocation of regulatory powers and the efficacy of the dual banking system (Division of Banking Sunset Review, 1993, p. 38). But given that existing information is insufficient to make a highly reliable estimate of the aggregate cost of regulations at commercial banks,[5] we must look to the "marketplace of charters" for possible answers. In other words, what bank officials as rational economic players decide to do given the choice of charters at their disposal.

Banking regulation at both the state and national level is funded through charges and assessments imposed on regulated institutions. The Colorado Division of Banking is funded by assessments based on total asset size. Table 2 below details (1) the actual assessment revenues of the Division for the last five fiscal years, (2) the projected cost to the industry if the institutions were operating as national charters, and (3) the aggregate savings enjoyed by Colorado state chartered institutions.

Table 2
Colorado Bank Assessments, FY 97-98 to FY 01-02

Annual Assessments					
Colorado Institutions*	**FY97/98**	**FY 98/99**	**FY 99/00**	**FY 00/01**	**FY 01/02**
State Chartered	$2,208,764	$2,245,901	$2,365,729	$2,611,215	$2,879,546
Cost if National Charter**	$4,087,309	$4,877,726	$5,248,815	$5,592,039	$5,617,597
Savings	**$1,878,545**	**$2,631,825**	**$2,883,086**	**$2,980,824**	**$2,738,051**

*Includes all state chartered banks, industrial bank, and trust companies.
**Based on the Office of the Comptroller of the Currency assessment calculation tables.

Clearly, one of the distinct benefits of obtaining a state charter is the lower operating cost (per institution regulated) in comparison to the Office of the Comptroller of the Currency (OCC), the regulator of nationally charted banks.

An analysis of state and national charters for Colorado and the nation reveals that over 65 percent of all institutions are state chartered. The comparison also reveals that a preponderance of smaller institutions opt for the state charter. Table 3 details the number of charter types for the preceding five years.

[5] Gregory Elliehausen, April, 1998. "The Cost of Banking Regulation: A Review of the Evidence," p. 29. Washington, DC: Board of Governors of the Federal Reserve System.

Table 3
National and State Bank Charters, June 30 1998 through June 30 2002

Number of Charter Types*					
Colorado	**6/30/98**	**6/30/99**	**6/30/00**	**6/30/01**	**6/30/02**
State Charters	139	131	129	125	123
State Charter <$100 M	89	79	75	74	69
National Charters	71	61	58	55	52
National <$100 M	49	43	38	31	26
State as Percent of Total	**66.2%**	**68.2%**	**69.0%**	**69.4%**	**70.3%**

United States	**6/30/98**	**6/30/99**	**6/30/00**	**6/30/01**	**6/30/02**
State Charters	6,436	6,264	6,174	6,002	5,862
State Charter <$100 M	4,316	4,064	3,874	3,636	3,387
National Charters	2,546	2,409	2,302	2,176	2,105
National <$100 M	1,329	1,237	1,162	1,049	988
State as Percent of Total	**71.7%**	**72.2%**	**72.8%**	**73.4%**	**73.6%**

*FDIC insured banks, trust companies and industrial bank (excludes nondepository trust companies)
Source: FDIC database: http://www2.fdic.gov/qbp/qbpSelect.asp?menuItem=STBL

Although the dual banking system does not appear to be highly efficient, it is highly effective in exerting downward pressure on chartering costs, fostering product innovation, and providing checks and balances in our system of financial regulation. In the words of Federal Reserve Chairman Alan Greenspan, "when there is no choice of regulatory agency, rigid policies and interfering regulatory micro-management can develop."[6] In the final analysis, it makes sense for the General Assembly to preserve and promote a dual federal and state banking system as is currently the case (see § 11-101-102, C.R.S.).

[6] Quoted in American Bankers Insurance Association. "The Benefits of Charter Choice: The Dual Banking System as a Case Study", p. 4.

Legal Framework

Federal Law

According to the Federal Deposit Insurance Corporation website, the most important federal laws that have affected the banking industry in the United States include:

- **National Bank Act of 1864** (Chapter 106, 13 Stat. 99).
  Established a national banking system and the chartering of national banks.

- **Federal Reserve Act of 1913** (Pub. L. 63-43, 38 Stat. 251, 12 U.S.C. 221).
  Established the Federal Reserve System as the central banking system of the U.S.

- **To Amend the National Banking Laws and the Federal Reserve Act** (Pub. L. 69-639, 44 Stat. 1224).
  Also known as The McFadden Act of 1927. Prohibited interstate banking.

- **Banking Act of 1933** (Pub. L. 73-66, 48 Stat. 162).
  Also known as the Glass-Steagall Act. Established the FDIC as a temporary agency. Separated commercial banking from investment banking, establishing them as separate lines of commerce.

- **Banking Act of 1935** (Pub. L. 74-305, 49 Stat. 684).
  Established the FDIC as a permanent agency of the government.

- **Federal Deposit Insurance Act of 1950** (Pub. L. 81-797, 64 Stat. 873).
  Revised and consolidated earlier FDIC legislation into one Act. Embodied the basic authority for the operation of the FDIC.

- **Bank Holding Company Act of 1956** (Pub. L. 84-511, 70 Stat. 133).
  Required Federal Reserve Board approval for the establishment of a bank holding company. Prohibited bank holding companies headquartered in one state from acquiring a bank in another state.

- **International Banking Act of 1978** (Pub. L. 95-369, 92 Stat. 607).
  Brought foreign banks within the federal regulatory framework. Required deposit insurance for branches of foreign banks engaged in retail deposit taking in the U.S.

- **Financial Institutions Regulatory and Interest Rate Control Act of 1978** (Pub. L. 95-630, 92 Stat. 3641).
  Also known as FIRIRCA. Created the Federal Financial Institutions Examination Council. Established limits and reporting requirements for bank insider transactions. Created major statutory provisions regarding electronic fund transfers.

- **Depository Institutions Deregulation and Monetary Control Act of 1980** (Pub. L. 96-221, 94 Stat. 132).
  Also known as DIDMCA. Established "NOW Accounts." Began the phase-out of interest rate ceilings on deposits. Established the Depository Institutions Deregulation Committee. Granted new powers to thrift institutions. Raised the deposit insurance ceiling to $100,000.

- **Depository Institutions Act of 1982** (Pub. L. 97-320, 96 Stat. 1469).
  Also known as Garn-St. Germain. Expanded FDIC powers to assist troubled banks. Established the Net Worth Certificate program. Expanded the powers of thrift institutions.

- **Competitive Equality Banking Act of 1987** (Pub. L. 100-86, 101 Stat. 552).
  Also known as CEBA. Established new standards for expedited funds availability. Recapitalized the Federal Savings & Loan Insurance Company (FSLIC). Expanded FDIC authority for open bank assistance transactions, including bridge banks.

- **Financial Institutions Reform, Recovery, and Enforcement Act of 1989** (Pub. L. 101-73, 103 Stat. 183).
  Also known as FIRREA. FIRREA's purpose was to restore the public's confidence in the savings and loan industry. FIRREA abolished the Federal Savings & Loan Insurance Corporation (FSLIC), and the FDIC was given the responsibility of insuring the deposits of thrift institutions in its place.

  The FDIC insurance fund created to cover thrifts was named the Savings Association Insurance Fund (SAIF), while the fund covering banks was called the Bank Insurance Fund (BIF).

  FIRREA also abolished the Federal Home Loan Bank Board. Two new agencies, the Federal Housing Finance Board (FHFB) and the Office of Thrift Supervision (OTS), were created to replace it.

  Finally, FIRREA created the Resolution Trust Corporation (RTC) as a temporary agency of the government. The RTC was given the responsibility of managing and disposing of the assets of failed institutions. An Oversight Board was created to provide supervisory authority over the policies of the RTC, and the Resolution Funding Corporation (RFC) was created to provide funding for RTC operations.

- **Crime Control Act of 1990** (Pub. L. 101-647, 104 Stat. 4789).
  Title XXV of the Crime Control Act, known as the Comprehensive Thrift and Bank Fraud Prosecution and Taxpayer Recovery Act of 1990, greatly expanded the authority of Federal regulators to combat financial fraud.

  This act prohibited undercapitalized banks from making golden parachute and other indemnification payments to institution-affiliated parties. It also increased penalties and prison time for those convicted of bank crimes, increased the powers and authority of the FDIC to take enforcement actions against institutions operating in an unsafe or unsound manner, and gave regulators new procedural powers to recover assets improperly diverted from financial institutions.

- **Federal Deposit Insurance Corporation Improvement Act of 1991** (Pub. L. 102-242, 105 Stat. 2236).
  Also known as FDICIA. FDICIA greatly increased the powers and authority of the FDIC. Major provisions recapitalized the Bank Insurance Fund and allowed the FDIC to strengthen the fund by borrowing from the Treasury.

The act mandated a least-cost resolution method and prompt resolution approach to problem and failing banks and ordered the creation of a risk-based deposit insurance assessment scheme. Brokered deposits and the solicitation of deposits were restricted, as were the non-bank activities of insured state banks. FDICIA created new supervisory and regulatory examination standards and put forth new capital requirements for banks. It also expanded prohibitions against insider activities and created new Truth in Savings provisions.

- **Housing and Community Development Act of 1992** (Pub. L. 102-550, 106 Stat. 3672).
  Established regulatory structure for government-sponsored enterprises (GSEs), combated money laundering, and provided regulatory relief to financial institutions.

- **RTC Completion Act** (Pub. L. 103-204, 107 Stat. 2369).
  Requires the RTC to adopt a series of management reforms and to implement provisions designed to improve the agency's record in providing business opportunities to minorities and women when issuing RTC contracts or selling assets. Expands the existing affordable housing programs of the RTC and the FDIC by broadening the potential affordable housing stock of the two agencies.

  Increases the statute of limitations on RTC civil lawsuits from three years to five, or to the period provided in state law, whichever is longer. In cases in which the statute of limitations has expired, claims can be revived for fraud and intentional misconduct resulting in unjust enrichment or substantial loss to the thrift. Provides final funding for the RTC and establishes a transition plan for transfer of RTC resources to the FDIC. The RTC's sunset date was set at December 31, 1995, at which time the FDIC assumed its conservatorship and receivership functions.

- **Riegle Community Development and Regulatory Improvement Act of 1994** (Pub. L. 103-325, 108 Stat. 2160)
  Established a Community Development Financial Institutions Fund, a wholly owned government corporation that would provide financial and technical assistance to CDFIs.

  Contains several provisions aimed at curbing the practice of "reverse redlining" in which non-bank lenders target low and moderate-income homeowners, minorities and the elderly for home equity loans on abusive terms. Relaxes capital requirements and other regulations to encourage the private sector secondary market for small business loans.

  Contains more than 50 provisions to reduce bank regulatory burden and paperwork requirements. Requires the Treasury Dept. to develop ways to substantially reduce the number of currency transactions filed by financial institutions. Contains provisions aimed at shoring up the National Flood Insurance Program.

- **Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994** (Pub. L. 103-328, 108 Stat. 2338).
  Permits adequately capitalized and managed bank holding companies to acquire banks in any state one year after enactment. Concentration limits apply and CRA evaluations by the Federal Reserve are required before acquisitions are approved. Beginning June 1, 1997, allows interstate mergers between adequately capitalized and managed banks, subject to concentration limits, state laws and CRA evaluations. Extends the statute of limitations to permit the FDIC and RTC to revive lawsuits that had expired under state statutes of limitations.

- **Economic Growth and Regulatory Paperwork Reduction Act of 1996** (Pub. L. 104-208, 110 Stat. 3009).
  Modified financial institution regulations, including regulations impeding the flow of credit from lending institutions to businesses and consumers. Amended the Truth in Lending Act and the Real Estate Settlement Procedures Act of 1974 to streamline the mortgage lending process.

  Amended the FDIA to eliminate or revise various application, notice, and recordkeeping requirements to reduce regulatory burden and the cost of credit. Amended the Fair Credit Reporting Act to strengthen consumer protections relating to credit reporting agency practices.

- **Gramm-Leach-Bliley Financial Modernization Act of 1999** (Pub. L. 106-102, 113 STAT 1338)
  Repeals last vestiges of the Glass-Steagall Act of 1933. Modifies portions of the Bank Holding Company Act (BHCA) to allow affiliations between banks and insurance underwriters. While preserving authority of states to regulate insurance, the act prohibits state actions that have the effect of preventing bank-affiliated firms from selling insurance on an equal basis with other insurance agents. Law creates a new financial holding company under section 4 of the BHCA, authorized to engage in: underwriting and selling insurance and securities, conducting both commercial and merchant banking, investing in and developing real estate and other "complimentary activities." There are limits on the kinds of non-financial activities these new entities may engage in. Allows national banks to underwrite municipal bonds.

  Restricts the disclosure of nonpublic customer information by financial institutions. All financial institutions must provide customers the opportunity to "opt-out" of the sharing of the customers' nonpublic information with unaffiliated third parties. The Act imposes criminal penalties on anyone who obtains customer information from a financial institution under false pretenses.

  Amends the Community Reinvestment Act to require that financial holding companies cannot be formed before their insured depository institutions receive and maintain a satisfactory CRA rating. Also requires public disclosure of bank-community CRA-related agreements. Grants some regulatory relief to small institutions in the shape of reducing the frequency of their CRA examinations if they have received outstanding or satisfactory ratings. Prohibits affiliations and acquisitions between commercial firms and unitary thrift institutions.

Makes significant changes in the operation of the Federal Home Loan Bank System, easing membership requirements and loosening restrictions on the use of FHLB funds.

Colorado Law

Summary of House Bill 03-1257

House Bill 03-1257, Concerning a Nonsubstantive Recodification of Colorado's Banking Laws, amended Title 11 of the Colorado Revised Statutes (C.R.S.) containing the "Colorado Banking Code." The comparative table in Appendix B is a useful means by which to cross-index the old banking code in relation to the recodified law.

State Banking Policy

Section 11-101-102, C.R.S., makes clear that it is state policy to protect the public interest by regulating the operations of all state banks so as to preserve and promote the security of deposits, a safe and sound banking system statewide, a dual federal and state banking system, and competition among financial services institutions.

Definitions

Section 11-101-401, C.R.S., sets out a total of sixty definitions concerning banking. Of these, the definition of what constitutes a bank is fundamental. A "bank" is defined as a state bank (other than an industrial bank), or a bank and trust company chartered by this state, or a national bank except those organized or chartered as a bank under the laws of any other jurisdiction or Chapter 2 of Title 12 of the United States Code. A "bank holding company" means any company that has direct or indirect control over any banking institution. "Financial institution" means any bank, bank holding company, industrial bank, industrial bank holding company, savings and loan association, federal savings bank, or thrift holding company. A "branch" means any branch bank, branch office, branch agency, additional office, or any branch place of business of a financial institution located in this state at which deposits are received, or checks are paid, or money is lent, or trust powers are exercised.

Division of Banking

Section 11-102-101, C.R.S., creates the Division of Banking (Division) and provides for its repeal. Section 11-102-102, C.R.S., makes clear that the Commissioner of Banking is the administrative head of the Division and is empowered to set administrative policy, including personnel matters, records, reports, systems, and procedures. In addition, the Commissioner is responsible for all examination and enforcement functions of the Division subject to the policy-making and rule-making authority of the Banking Board. The Commissioner may delegate to any officer or employee of the Division any of the Commissioner's powers and may designate any officer or employee of the division to perform any of the Commissioner's duties.

Banking Board

Section 11-102-103, C.R.S., creates the Banking Board (Board). The required composition of this body is as follows:

- Four members who are executive officers of state banks with at least five years of practical experience
- One member who is an executive officer of an industrial bank
- One member who is an executive officer of a trust company
- Two members who have experience in finance and serve as public members

Of the eight members, not more than four can be of the same major political party. At all times, at least one member must reside west of the continental divide. Members are appointed by the Governor with the consent of a majority of the Senate. The term of office for each member is four years. The Board must meet at least once in each calendar month. The chairman of the Board may call additional meetings upon at least seventy-two hours' notice to all members of the Board and must do so upon the request of two members. All members of the Board are subject to immediate call in the event of an emergency. Four members of the Board constitute a quorum, and action taken by a majority of those present at any meeting at which a quorum is present represents official Board action.

Powers of the Banking Board

Section 11-102-104, C.R.S., sets out the powers of the Banking Board. The Board is the policy-making and rule-making authority for the Division of Banking and has the power to make, modify, reverse, and vacate rules for the proper enforcement and administration of the Colorado Banking Code and the "Public Deposit Protection Act." In addition, the Board is empowered to make, promulgate, alter, amend, or revise reasonable rules as may be necessary for the enforcement and execution of the provisions of the "Money Order Act." In addition, the Board can:

- Make all final decisions with respect to bank ownership, including chartering and conversions, mergers, acquisitions, and change of control;
- Make all final decisions with respect to the taking of possession, liquidation, or reorganization of banks and the emergency grant of new charters and branch facilities;
- Make all final decisions with respect to requests to exercise trust, fiduciary, and agency powers;
- To prohibit the taking of deposits or to restrict the withdrawal of deposits, or both, from any one or more state banks when the Banking Board finds such a restriction necessary for the proper protection of depositors;
- To affirm, modify, reverse, vacate, or stay the enforcement of any order of or ruling made by a hearing officer or the Bank Commissioner;
- To order any person in violation to cease engaging in any unsound banking practice, to impose civil money penalties, to suspend or remove a director or officer, and to take other authorized enforcement action; and,

- To establish annually fees and assessments as are necessary to generate the moneys appropriated by the General Assembly for the Division.

Members of the Board, officers, and employees of the Division are exempt from liability in any civil action for damages for any act done or omitted in good faith in performing the functions of his or her office (§ 11-102-502, C.R.S.).

Bank Examinations

Section 11-102-301, C.R.S., empowers the Commissioner to examine the books and records of every state bank as often as deemed advisable and to the extent required by the Banking Board, and to file in his or her office a correct report in detail disclosing the results of such examination, and requires him or her to mail a copy of such report to the bank examined. Similarly, the Commissioner may examine any electronic data processing centers of a state bank. In lieu of any examination, the Commissioner may accept an audit for the previous fiscal year prepared by an independent certified public accountant, independent registered accountant, or other independent qualified person. If the Commissioner accepts an audit prepared by such independent person, the costs of the audit remain the obligation of the controlling shareholder or affiliate.

Section 11-102-302, C.R.S., requires every state bank to produce and file with the Banking Board not less than three reports during each calendar year in a form prescribed by the Board.

Confidentiality of Information

Section 11-102-306, C.R.S., provides for the confidentiality of information. It requires the Banking Board, the Bank Commissioner, and all deputies and employees of the Division not to divulge any information acquired by them in the discharge of their duties except insofar as disclosure may be rendered necessary by law. The Banking Board, the Commissioner, and their designees may exchange information with the United States Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, the Federal Home Loan Bank in which an institution is a member or is making an application to become a member, the Executive Director of the Department of Regulatory Agencies, the Division of Financial Services, and banking regulatory agencies of other states, subject to any confidentiality agreement entered into between the Banking Board or the Commissioner and the United States Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, or the Federal Home Loan Bank in which an institution is a member or is making an application to become a member. There are additional exemptions.

Fees and Assessments

Section 11-102-401, C.R.S., authorizes the Banking Board to establish fees and assessments annually. Assessments may be made more frequently than annually at the discretion of the Banking Board. For the fiscal year beginning July 1, 2003, and for each fiscal year thereafter, the Banking Board must establish an assessment to be collected at least semiannually in such amounts as are sufficient to generate the moneys appropriated by the general assembly to the Division of Banking for each such fiscal year. The Banking Board may also assess filing fees to banks and bank holding companies outside of Colorado that are seeking to acquire a bank or bank holding company in Colorado in such amount as determined to be sufficient to reimburse the state for the cost of administration (§ 11-102-402, C.R.S.).

Division of Banking Cash Fund

The Division of Banking cash fund is created by way of section 11-102-403, C.R.S. All fees and assessments collected by the Banking Board must be transmitted to the State Treasurer, who credits the same to the Division of Banking cash fund established in the state treasury by this provision. All moneys in the fund are subject to appropriation by the General Assembly for the direct and indirect costs of the activities of the Banking Board and the Division. All interest derived from the deposit and investment of moneys in the fund are credited to the fund. Any moneys not appropriated must remain in the fund and not be transferred or revert to the general fund of the state at the end of any fiscal year.

Civil Penalties

Section 11-102-503, C.R.S., authorizes the Banking Board to assess civil money penalties. After notice and a hearing, and after making a determination that no other appropriate governmental agency has taken similar action against such person for the same act or practice, the Banking Board may assess against and collect a civil penalty from any state bank that, or any executive officer, director, employee, agent, or other person participating in the conduct of the affairs of such bank who, violates or knowingly permits any person to violate any of the provisions of the Banking Code, or engages or participates in any unsafe or unsound practice in connection with a bank. Violations may include, but are not limited to: making, or causing to be made, delinquent payment of assessments; submitting, or causing to be submitted, delinquent reports, including but not limited to call reports; or knowingly submitting, or causing to be submitted, to the Banking Board any report or statement that contains materially false or misleading information.

The Banking Board is empowered to determine the amount of any civil money penalty assessed against any executive officer, director, employee, agent, or other person participating in the affairs of a bank, except as expressly limited by this code. In determining the amount of the civil money penalty to be assessed, the Banking Board shall consider the good faith of the person assessed, the gravity of the violation, any previous violations by the person assessed, the nature and extent of any past violations, and such other matters as the Banking Board may deem appropriate, except that the civil money penalty must not exceed one thousand dollars per day for each day the person assessed remains in violation. Civil money penalties are payable within 30 days after the notice of assessment.

General Corporate Powers of State Banks

The general corporate powers of state banks are set out in section 11-103-101, C.R.S., In addition to its other powers, a state bank that is authorized by its charter to exercise trust powers, upon proper qualification, has the power to act as a fiduciary in any capacity. It may also act as registrar, transfer agent, fiscal agent, or attorney-in-fact and have the power to receive, manage, and apply sinking funds. Every state bank that is authorized by its charter to exercise trust powers must create and file with the Commissioner an annual report of trust assets and such other reports as the Banking Board may require by rule on such forms as may be prescribed by the Board (§ 11-103-102, C.R.S.).

Capital Required Of Banks

The capital required of banks is established by way of section 11-103-201, C.R.S. The Banking Board is mandated to establish by rule the capital standards, guidelines, and methods for measuring capital. The Banking Board may also define for specific purposes "capital," "capital adequacy," "capital inadequacy," and other related terms for state banks. In promulgating such rules, the Board must consider all relevant factors, including, without limitation, the policies set by legislative declaration, and relevant federal laws and rules. Each bank subject to the Banking Code must at all times comply with the capital rules promulgated by the Banking Board. If the Banking Board determines that an inadequacy of capital exists, the Commissioner, with the approval of the Board, may direct a state bank to levy an assessment in a designated amount upon the holders of record of common stock to remedy the inadequacy of capital. If the Banking Board determines that the capital or reserves of any bank are inadequate, the Board may order the bank not to make new loans or discounts (§ 11-103-202, C.R.S.).

State Charter Requirements

Section 11-103-303, C.R.S., sets out the requirements for banks to obtain a state charter. After the capital stock has been fully subscribed, prospective incorporators must make application to the Banking Board for a charter to include its proposed articles of incorporation in duplicate, and an application for a charter in such form and containing such information as the Board may require. Not more than 40 days after a properly filed application, the Banking Board must mail notice of such filing to each bank within a three-mile radius of the location of the proposed bank and to such other persons or banks as the Board may designate.

Within 60 days following the filing of the completed application for charter, the Commissioner must make or cause to be made a careful investigation to determine that the applicant has proceeded in a lawful manner; that the name is not deceptively similar to that of another bank or otherwise misleading; that the proposed capital satisfies Banking Board standards and guidelines; and that the persons who will serve as directors or officers possess the qualifications and experience required, as well as a financial status consistent with their responsibilities and duties. The Banking Board within six months after the filing of an application for charter must hold a public hearing to consider the application, except that the Board may postpone such hearing for good cause. At such hearing, the applicant must prove that the proposed bank will serve a public need and advantage in the community that

the bank will serve; and, that the volume of business in the community that the proposed bank will serve is such that profitable operation of the bank may be reasonably projected (§ 11-103-304, C.R.S.).

In addition, the Banking Board must make a statement declaring that the application and proposed articles of incorporation are available for inspection in the office of the Board. The Banking Board must also cause such notice to be published at least one time not less than 20 days prior to the date fixed for such hearing in a newspaper of general circulation within the community in which the proposed bank is to be located. Within one hundred twenty days following the date of conclusion of the hearing, the Board must issue a written order requiring the Commissioner to grant a charter if a majority of the Banking Board finds that relevant requirements have been met. The Banking Board must make execution of its order to grant a charter contingent upon the proposed bank making a bona fide application for membership in the Federal Deposit Insurance Corporation, or the Federal Reserve System (§ 11-103-304, C.R.S.).

Financial Reports

Among the most important provisions of section 11-103-502, C.R.S., are those relating to financial reporting. The board of directors of a bank is required to cause the financial statements of their state chartered bank to be prepared in accordance with generally accepted accounting principles. These must be consistently applied, except as the Banking Board may otherwise provide in order to establish regulatory and competitive parity. In addition, the board of bank directors must cause an audit to be completed by an accounting firm composed of certified public accountants, or a directors' examination by a public accountant or any other independent person at least annually, but at intervals of not more than fifteen months, as may be required by the Banking Board or its rules. The Board must adopt rules regarding the qualifications of such public accountant and other independent person or persons, who shall assume the responsibility for due care in such director's examinations. The Banking Board's rules must also establish the scope of such directors' examinations, which must include safeguards to insure that such examinations adequately describe the financial condition of the financial institution. The Banking Board may require an audit to be completed by an accounting firm composed of certified public accountants under certain circumstances. A report of the audit or directors' examination and any related management letters and documents must be completed and submitted to the Banking Board within the time periods, form, and containing such information as the Board may require in its rules.

Mergers and Conversions

Upon approval of the Banking Board, banks may be merged with, or converted into, a resulting state bank, except that the action by a constituent national bank shall be taken in the manner prescribed by, and shall be subject to, any limitation or requirements imposed by any law of the United States, which law also governs the rights of its dissenting shareholders. After approval by the board of directors of each constituent bank, the merger

agreement must be submitted to the Banking Board for approval, together with certified copies of the authorizing resolutions of the several boards of directors showing approval by a majority of the entire board and evidence of proper action by the board of directors of any constituent national bank (§§ 11-103-701; 11-103-703, C.R.S).

Section 11-103-707, C.R.S., sets out the procedures for converting from a state chartered to a nationally chartered bank and vice versa. There is no prohibition against a state bank converting into a national bank upon compliance with the laws of the United States. Upon completion of such conversion, however, it must surrender its charter as a state bank. A national bank located in Colorado that follows the procedure prescribed by federal law to convert into a state bank must be granted a state charter if it meets the requirements for the incorporation of a state bank. The converted bank is to be considered the same business and corporate entity as the converting bank with all of the rights, powers, and duties of the converting bank except as limited by the charter and bylaws of the resulting bank. It may use the name of the converting bank whenever it can do any act under such name more conveniently.

If a constituent bank has assets that do not conform to the requirements of state law for the resulting bank, or if a converting national bank has assets that do not conform to the requirements of a state law for the converted state bank, or if, in either case, there are business activities that are not permitted for the resulting or converted state bank, the Banking Board may permit a reasonable time to conform with state law. Any state bank may sell to any other bank all, or substantially all, of the selling bank assets and business, or all, or substantially all, of the assets and business of any department of the selling bank (§§ 11-103-708; 11-103-709, C.R.S.).

Voluntary Liquidation of State Banks

Section 11-103-801, C.R.S., covers the voluntary liquidation of state banks. With the approval of the Banking Board, a state bank may liquidate and dissolve. The Board must grant such approval if it appears that the proposal to liquidate and dissolve has been approved by a vote of two-thirds of the outstanding voting stock at a meeting called for that purpose, and that the capital of the state bank is adequate and such state bank has sufficient liquid assets to pay off depositors and creditors immediately. Any assets remaining after the discharge of all obligations must be distributed to the stockholders in accordance with their respective interests. No such distribution is to be made before all claims of depositors and creditors have been paid or, in the case of any disputed claim, the bank has transmitted to the Board a sum adequate to meet any liability that may be judicially determined and any funds payable to a depositor or creditor and unclaimed have been transmitted to the Banking Board.

Involuntary Liquidation of State Banks

Involuntary liquidation is addressed in section 11-103-802, C.R.S. The Banking Board may take possession of a state bank if, after a hearing before the Banking Board, the Board finds:

- The bank's capital is inadequate or it is otherwise in an unsound condition;

- The bank's business is being conducted in an unlawful or unsound manner;
- The bank is unable to continue normal operations;
- Examination of the bank has been obstructed or impeded; and,
- Control of the bank has been assumed by any person or persons convicted of fraud or a felony in this state or any other jurisdiction, or by any partnership, association, or corporation controlled, directly or indirectly, by any person so convicted.

When the Commissioner takes possession of a state bank, he or she becomes vested with the full and exclusive power of management and control, including the power to continue or to discontinue the business; to stop or to limit the payment of its obligations; to employ any necessary assistants, including legal counsel; to execute any instrument in the name of the bank; to commence, defend, and conduct in its name any action or proceeding to which it may be a party; to terminate the possession by restoring the bank to its board of directors; and reorganize or liquidate the bank. As soon as practicable after taking possession, the Commissioner must make an inventory of the assets and file a copy of these with the court in which the notice of possession was filed.

If, in the opinion of the Banking Board, an emergency exists that may result in serious losses to the depositors, it may take possession of a state bank and may immediately appoint the Federal Deposit Insurance Corporation (FDIC) or its successor as liquidator without notice of a hearing (§ 11-103-802(3)(b), C.R.S.). The FDIC, or its successor, is authorized by section 11-103-805, C.R.S., to act without bond as liquidator of any banking institution with insured deposits. After being notified in writing of the acceptance of such an appointment, the Commissioner must file in the office of the clerk and recorder in the county in which the bank is situated a certificate evidencing the appointment of the FDIC. Upon such an appointment, the possession of all the assets, business, and all the property of such bank, wheresoever situated, are deemed transferred from the liquidated bank and the Banking Board to the FDIC.

Colorado Bank Holding Companies

A Colorado bank holding company may acquire control of out-of-state bank holding companies and out-of-state banks. Similarly, subject to certain limitations, an out-of-state bank holding company may acquire control of Colorado financial institutions. Concerning interstate banking, no bank or bank holding company may conduct interstate branching in Colorado, or acquire control, directly or indirectly, of any Colorado financial institution without first obtaining a certificate of compliance from the Banking Board (§ 11-104-202, C.R.S). Any bank holding company controlling any other bank holding company or bank is subject to the jurisdiction of the Banking Board with respect to its operations and affairs in the State of Colorado (§ 11-104-203, C.R.S).

Banking Practices

Section 11-105-101, C.R.S., sets out standards for banking practices. Except as provided in the federal Gramm-Leach-Bliley Financial Modernization Act of 1999 (Pub. L. 106-102, 113 Stat. 1338), it is unlawful for a bank, or an officer, director, employee, or affiliate of a bank, to engage in the business of issuing, floating, underwriting, distributing, or promoting the sale of stocks, bonds, or other securities, or to be an officer, trustee, director, employee, stockholder, or partner of any person engaged principally in any such business. In addition, no officer, director, employee, or agent of a state bank may maintain, or authorize any bank account that, to his or her knowledge, does not conform to the requirements of the Banking Code, the Commissioner, or the Banking Board.

Demand, Savings, and Time Deposit Accounts

Section 11-105-102, C.R.S., establishes that a state bank may maintain demand, savings, and time deposit accounts and any type of account that a national bank provides. The Banking Board may by rule establish the maximum annual rate of interest that a state bank may pay on any type of deposit or account. In the absence of such rule, a state bank is subject only to applicable federal law in the payment of interest. A bank may accept money for transmission, may transmit money, and buy and sell foreign exchange to the extent necessary to meet the needs of customers (§ 11-105-108, C.R.S.).

Bank Investments

The type of bank investments that a state bank may engage in are set out in section 11-105-304, C.R.S. State banks are permitted to purchase shares in small business investment companies, directly engage in activities that are primarily investments in real estate, invest in the securities of investment companies and trusts, and enter into other types of investments. A state bank may also invest in any obligation, exercise such powers, and engage in such activities that such bank could legally acquire, exercise, and engage in were it operating as a national bank at the time such investment was made. In addition, a state bank may invest in fixed assets of the bank or the stock or obligations of any corporation holding such fixed assets, or may make loans to, or upon the security of the stock of any such corporation, but the aggregate of all such investments and loans must not exceed 100 percent of the bank's capital, as provided in the rules of the Banking Board (§ 11-105-402, C.R.S.).

Bank Branches

Section 11-105-602, C.R.S., permits the conversion of financial institutions to branches, and the operation of bank branches. Any bank or industrial bank that has its principal place of business in Colorado, upon 30 days' prior written notice to the Banking Board, or any savings and loan association that has its principal place of business in this state, upon 30 days' prior written notice to the State Commissioner of Financial Services, may establish one or more *de novo* branches anywhere in this state. The Board and the Commissioner must adopt policies and procedures by rule no more restrictive than federal regulatory policies and procedures relative to application and approval of branches. Any bank subsidiary of a bank holding company may receive deposits, renew time deposits, close

loans, service loans, and receive payments on loans and other obligations as an agent for an affiliate financial institution, as such authority is set forth in section 101(d) of the federal Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. Notwithstanding any other provision of law, a bank acting as an agent in accordance with this provision is not to be considered to be a branch of the affiliate (§ 11-105-604,C.R.S.).

Criminal Offenses

Section 11-107-101, C.R.S., makes clear that it a criminal offense to engage in an unauthorized banking business. It is unlawful for an affiliate of a state bank, or for an officer, director, or employee of a state bank to solicit, accept, or agree to accept, directly or indirectly, from any person other than the institution, any gratuity, compensation, or other personal benefit for any action taken by the institution, or for endeavoring to procure any such action. Further, there is a prohibition against having any interest, direct or indirect, in the purchase at less than its face value of any evidence of indebtedness issued by the institution (§ 11-107-104,C.R.S.). Similarly, it is a criminal offense for an officer, director, employee, attorney, or agent of a state bank with intent to deceive, to make any false or misleading statement or entry, or omit any statement or entry that should be made in any book, account, report, or statement of the institution (§ 11-107-105, C.R.S.). Embezzlement or misappropriation of funds is prohibited by way of section 11-107-107, C.R.S., which holds that it is a criminal offense for any officer, director, shareholder, or employee of any bank to directly or indirectly embezzle, abstract, or misapply, or cause to be embezzled, abstracted, or misapplied, any of the funds or securities or other property of or under the control of the bank with intent to deceive, injure, cheat, wrong, or defraud any person.

According to section 11-107-108, C.R.S., any person responsible for an act or omission expressly declared to be a criminal offense by the Banking Code is guilty of a misdemeanor and, upon conviction, is punishable by a fine of not more than $1,000, or by imprisonment in the county jail for not more than one year, or both. If the act or omission was intended to defraud, such a person commits a class 6 felony and is punishable as provided in section 18-1.3-401, C.R.S. If a violation may cause substantial injury to the institution, or to the depositors, creditors, or stockholders, the district court in and for the county in which the bank is located may, upon the suit of the Banking Board, issue an injunction restraining such violation. (§ 11-107-110, C.R.S.).

Industrial Banks

Article 108 of Title 11 of the Colorado Revised Statutes (§§11-108-101 to 11-108-803) addresses industrial banks. The powers, duties, and functions of the Banking Board and Commissioner apply to industrial banks (§ 11-108-102, C.R.S.).

One of the main differences between banks and industrial banks is that the latter are prohibited from accepting demand deposits that the depositor may withdraw by check or similar means for payment to third parties (§ 11-108-204, C.R.S.). Every industrial bank duly organized and chartered has the powers granted general business corporations by the laws of the State of Colorado to the extent these are not inconsistent with the Banking Code (§ 11-108-201, C.R.S.).

Section 11-108-202, C.R.S., allows industrial banks to purchase and carry a variety of bonds, secured or unsecured notes, mortgages, contracts, acceptances, bills of exchange, or trust receipts. All assets and funds of an industrial bank must at all times be maintained within the Unites States and in legal investments. Industrial banks may pay interest on savings deposits, certificates of deposit, contracts, or agreements at a rate, without regard to compounding, not to exceed one-half percent per annum greater than the rates of interest that any national or state bank, savings and loan association, or building and loan association in the state is permitted by law to pay on the same type of savings deposit, certificate of deposit, contract, or agreement, whichever is greater.

In addition to being subject to Colorado's corporation laws, industrial banks must be examined as often as is deemed advisable by the Commissioner and to the extent required by the Banking Board. The cost of the examination is borne by the industrial bank. Similarly, electronic data processing centers of an industrial bank or any electronic processing centers that serve an industrial bank are subject to examination (§ 11-108-401, C.R.S.).

Trust Companies

Article 109 of Title 11 of the Colorado Revised Statutes (§§11-109-101 to 11-109-907) addresses trust companies. A "trust institution" means a trust company, a federal or state chartered bank with trust powers, or a trust company chartered under the laws of another state. Trust companies are empowered to act as a fiduciary to accept or execute trusts, including to receive money or other property in the capacity of trustee for investment in real or personal property (§11-109-101, C.R.S.). The powers, duties, and functions of the Banking Board and Commissioner apply to trust companies (§11-109-103,C.R.S.).

Section 11-109-102, C.R.S., makes use of the words "trust" or "trust company" unlawful for any person, firm, association, or corporation in the conduct of its business in such a manner as is likely to cause the public to be confused, deceived, or mistaken that such entity has been authorized to transact business as a regulated financial institution unless such entity is organized under the "Colorado Banking Code". This requirement does not apply to state banks with trust powers, national banking associations located in Colorado that have trust powers, and trust companies incorporated in Colorado.

Section 11-109-104, C.R.S., empowers the Commissioner to examine the books and records of every trust company as often as deemed advisable and to the extent required by the Banking Board. In addition, he or she is required to make and file a correct report in detail disclosing the results of such examination; and to mail a copy of such report to the trust company examined. Similarly, the Commissioner is empowered to examine any electronic data processing centers of a trust company or any electronic data processing centers that serve a trust company, without regard to the location of the electronic data processing center.

Summary of Risk- Based Examination Scheduling Policy

Policy No. 80-1 is one of the most important adopted by the State Banking Board. It establishes the types and frequencies of examinations conducted by the Division of Banking based on the condition of the financial institutions under its jurisdiction. For purposes of this policy, “financial institutions“ means commercial banks, industrial banks, trust companies, money order companies, information technology service providers, and foreign capital depositories. Examinations are based on prior composite ratings ranging from one through five, with “1” being the best and “5” the worst.

The scope of examination may be full or targeted. A full-scope examination covers all aspects of the function being examined in sufficient depth to assign a rating. A target examination, on the other hand, covers less than a full scope examination and a rating is not assigned. This policy makes clear that the Division will make every effort to coordinate examination schedules with the Federal Deposit Insurance Corporation and the Federal Reserve Bank. In addition, semi-annual examination coordination meetings must be held with federal regulators.

Mandatory safety and soundness examinations at commercial banks, industrial banks, and depository trust companies are based on the following criteria:

- New state charters must undergo a target examination within the first four months of operation and full scope examinations at 12-month intervals for the first three years of operation on an alternating basis with federal regulators;
- Institutions with assets less than $250 million and a composite rating of one or two must undergo a full scope examination at 18-month intervals on an alternating basis with federal regulators;
- Institutions with assets greater than $250 million and a composite rating of one or two must undergo a full scope examination at twelve month intervals on an alternating basis with federal regulators; and,
- Institutions with composite ratings of three, four, or five must undergo a full scope examination at least annually.

Mandatory safety and soundness examinations of non-depository trust companies are similar to those of banks, except that the asset size criterion is not employed. All foreign capital depositories must undergo a full scope examination every 12 months regardless of their composite rating.

Mandatory Public Deposit Protection Act (PDPA) examinations at commercial banks and industrial banks must occur within the first four months of accepting public deposits. Thereafter, institutions with a composite rating of one or two must undergo a targeted examination every 36 months, while those institutions with a rating of three must be on a 24-month examination schedule. If these institutions also have total public deposits in excess of 10 percent of the aggregate public deposits, they must undergo a targeted examination every 12 months. Commercial banks and industrial banks with composite ratings of four or five must undergo a full-scale examination at least annually. Targeted escrow PDPA examinations at new PDPA escrow institutions must occur within the first four months of assuming this role. Thereafter, full scope examinations are to occur every 24 months.

The scheduling and scope of discretionary examinations are determined by the Commissioner, or a designee, with input from the Director of Examinations based on off-site monitoring, or on any other information which may indicate a problem, or potential problem, requiring a discretionary examination.

Policy No. 80-1, was most recently revised on June 19, 2003.

Program Description and Administration

The mission of the Colorado Division of Banking (Division) is to serve and protect the public interest by promoting a safe and sound financial institutions industry through continuous quality regulation and supervision. More specifically, the Division is responsible for public deposit protection and the regulation of state-chartered commercial banks, industrial banks, trust companies, money transmitters, and money-order companies. The Division holds charter and license application hearings and issues rules and regulations affecting regulated institutions. Division staff conduct examinations of state-chartered institutions and licensees and examine the following functions in financial institutions: Public Deposit Protection Act compliance, trust departments, electronic funds transfer, electronic data processing, and Uniform Consumer Credit Code compliance. The Division also works closely with the Federal Reserve Bank and the Federal Deposit Insurance Corporation concerning the regulation of commercial and industrial banks and certain federally mandated insured trust companies.

The eight-member Colorado State Banking Board is the policy and rulemaking authority for the Division. The Banking Board consists of four members who are executive officers of state banks, an executive officer of an industrial bank, an executive officer of a trust company, and two public members. The State Bank Commissioner is the administrative head of the Division, responsible for the day-to-day operations of the Division, including personnel matters, records, reports, systems, and procedures. The Commissioner is also responsible for all examination and enforcement functions of the Division, subject to the policy-making and rulemaking authority of the Banking Board.

Under the direction of the Commissioner, the Division is organized into four main units: Examinations; Operations; Public Deposit Protection Act Administration; and Applications and Complaints. The Division currently has 38.5 authorized employees, 26.5 of whom are in the Financial Credit Examiner (FCE) category. Of the 26.5 FCE classifications, 20 are field examiners, four are portfolio managers, one manages applications and complaints, one is the Director of Examinations, and there is .5 allocation for foreign capital depository examination. The Division also employs two electronic data processing auditors. Other positions include an Operations Manager and administrative and support staff. A more detailed description of the main organizational units follows.

The size of the regulated community under the jurisdiction of the Division is depicted in Table 4. A detailed listing of these institutions together with relevant contact information may be found in the Commissioner's annual report to the Governor. Growth trends in Colorado's banking industry as represented by new charters are depicted in Table 5 below.

Table 4
Regulated Institutions in Colorado, 1998-2002

Number of Regulated Entities*	12/31/98	12/31/99	12/31/00	12/31/01	12/31/02
Commercial Banks	123	121	117	116	114
Industrial Banks	5	4	4	5	4
Trust Companies	10	10	9	10	10
Total	**138**	**135**	**130**	**131**	**128**

*Excludes money transmitters, debt adjusters (sunsetted in 2000), third party providers, escrow companies, and national banks examined for PDPA compliance.

For the period under review, the total number of institutions under supervision (excluding money transmitters) declined from 138 to 128. In general, the reduction in the number of Colorado institutions mirrors the national trend of increased bank consolidation. The total assets of Colorado institutions, however, increased from slightly less than $16 billion to more than $21 billion in the same period.

Table 5
New Charters by Type of Institution, 1998-2002

New Charters*	12/31/98	12/31/99	12/31/00	12/31/01	12/31/02
Commercial Banks	7	2	1	4	1
Industrial Banks	0	0	0	1	0
Trust Companies	0	0	0	2	0
Total	**7**	**2**	**1**	**7**	**1**

*New charters are reported in the year the institution was granted a charter and opened for business. In some instances, the Banking Board approval may have occurred in the preceding year.

The number of new charters approved on an annual basis may appear relatively low, but is representative of a stable banking industry and the significant organizational costs and capitalization requirements incurred in organizing a *de novo* institution. The $4 million minimum initial capital requirement generally required for FDIC insurance curtails the number of applicants, but provides for more resilient institutions with a higher probability of success.

In fiscal year 01-02, the Division carried out its mission with 38.5 authorized full-time equivalent employees (FTE) and expenditures amounting to $3,195,854. Appropriations, expenditures, and authorized FTEs for the previous five fiscal years are shown in Table 6 below.

Table 6
Division of Banking Budgetary Information and Staffing, FY 97-98 to FY 01-02

	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Appropriations	$3,055,955	$3,076,895	$3,189,026	$3,272,446	$3,316,101
Actual Expenditures	$2,791,187	$2,980,860	$2,962,289	$3,260,783	$3,195,854
Authorized FTE	40.0	38.0	38.5	38.5	38.5

The figures in Table 6 are aggregate numbers and FTE for the Division of Banking, inclusive of all programs.

In addition to state mandated reviews, the Division of Banking's operations are independently evaluated by means of an accreditation process administered by the Conference of State Bank Supervisors (CSBS). The accreditation program involves annual self assessments according to a CSBS developed questionnaire and rating system, supplemented by an on-site review conducted by CSBS every five years. The Division was re-accredited in 2001. The Division's procedures, products, and personnel were evaluated and rated. This process constitutes an independent review of Division operations, as well as a method by which to identify areas for improvement and as a comparison to other state banking departments. CSBS accreditation is one factor used by federal regulatory agencies in determining the acceptability of state examinations pursuant to interagency agreements and as a basis for alternating state/federal examinations.

Each unit of the Division of Banking is described according to its function next.

Examinations Unit

Examinations are the core function of the Division of Banking. The examinations unit is responsible for overseeing the regulation of state chartered commercial and industrial banks, trust companies, money order companies, money transmitters, and foreign capital depositories. Within the examinations unit, supervisory and examination responsibilities are assigned to four portfolio managers. The portfolio managers supervise examination teams and are the primary agency representatives to regulated institutions.

Based on the risk profile of the regulated institution, the scope of the examination is determined and examination programs, procedures, or both are selected. Composite ratings are assigned to the institution based on the examination findings. An important tool in assessing the risk profile of banks is the CAMELS rating system. Division examiners review six critical aspects of a bank's operations under this rating system. The individual CAMELS criteria are:

- Capital adequacy
- Asset quality
- Management and administrative ability
- Earnings level and quality

- Liquidity level
- Sensitivity to market risk

This risk-focused examination process requires Division examiners to first perform a risk assessment of a state bank before beginning any on-site supervisory activities. Risk assessments involve identifying the significant activities of a bank, determining the risks inherent in those activities, and undertaking a preliminary assessment of the procedures a bank has in place to identify, measure, monitor, and manage these risks. Examiners then use a bank's own risk assessment to direct their examination efforts toward the areas of greatest risk to the institution. For banks with sound risk-management procedures, examiners utilize internal risk assessments more extensively rather than performing extensive supervisory tests.

Banks are rated from "1" to "5" on each of the CAMELS criteria. A rating of "1" is the highest and indicates the best risk-management practices, strongest performance, and least degree of supervisory concern. On the other hand, a "'5" is the lowest rating and implies inadequate risk-management practices, weakest performance, and highest level of regulatory concern. Bank assessments are based on each bank's total assets, including a 25 percent surcharge for banks rated "4" or "5."

In addition to the CAMELS ratings, and according to Banking Board Policy 80-1, asset size, capital strength, *de novo* status, and outstanding enforcement action are all used in establishing examination frequency. The Division has also entered into interagency examination agreements with federal banking authorities (FDIC and Federal Reserve Bank), as well as other state regulators. The federal agreements provide for alternating examination schedules, or which agency has lead authority, or both. For example, a small, well-managed, well capitalized commercial bank, on an 18-month examination cycle would be examined by the Division in January 2000, by the FDIC in July 2001, and again by the Division in January 2003.

Table 7
Safety and Soundness exams, FY 97-98 to FY 01-02

Type of Institution	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Banks	57	43	58	45	53
Industrial Banks	1	1	3	3	1
Trust Companies	7	7	7	8	9
Total	**65**	**51**	**68**	**56**	**63**

In addition to safety and soundness exams, the Division performs information technology exams, Public Deposit Protection Act (PDPA) exams, and trust department exams. Table 8 shows the number of information technology exams conducted over a five-year period.

Table 8
Information Technology Exams, FY 97-98 to FY 01-02

Type of Institution	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Banks	20	12	5	19	10
Industrial Banks	1	0	0	2	0
Trust Companies	1	3	2	0	3
Third-Party Providers	11	5	4	7	7
Total	**33**	**20**	**11**	**28**	**20**

In the period leading to 2000, an unusually high number of information technology examinations were performed because target Y2K examinations were required to be conducted on all institutions with in-house data processing prior to the beginning of that year. Those special examinations were conducted over and above the normally required technology examinations for that year. After January 1, 2000 was successfully ushered in, the Division discontinued conducting those special target information technology examinations, which were meant to ensure that those banks' systems were prepared for the Year 2000 conversion.

Table 9 depicts trust department exams for the period under review. Concerning the lack of examinations at non-depository trust companies, separate trust department examinations are not conducted at these institutions. Rather, the trust examination procedures are combined with the safety and soundness procedures at these establishments, with a single examination report issued.

Table 9
Trust Department Exams, FY 97-98 to FY 01-02

Type of Institution	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Banks	9	8	8	7	6
Industrial Banks*	0	0	0	0	0
Depository Trust Co.	1	2	2	0	2
Non-depository Trust Co.	0	0	0	0	0
Total	**10**	**10**	**10**	**7**	**8**

* There were no industrial banks authorized to exercise trust powers during the review period.

All significant problems identified during any type of examination are discussed with Division staff, as well as the institution's management. Required corrective actions are outlined in the report of examination and reiterated in the transmittal letter with a specified response date that is submitted to the institution's board of directors. If the violations or other circumstances are serious enough, enforcement action (informal or formal) may be pursued. If action is initiated, examination staff monitor the institution's compliance with the enforcement action. This may entail receiving and evaluating the institution's response; receiving and evaluating progress reports (if required by the action); and, if deemed appropriate, visiting the institution to verify its response.

To ensure that examination staff are kept apprised of changes in the financial condition of regulatory institutions between examinations, a supervisory monitoring program has been established. The primary objective of monitoring is to facilitate effective and timely regulatory oversight through financial analysis and reporting which stresses early detection of potential and actual problems. Through the use of various reports and other information, all Division regulated institutions are subject to off-site monitoring each quarter. The examiner submits completed monitoring reports to the caseload manager along with any recommended follow-up. The caseload manager reviews and signs-off on the reports and initiates appropriate follow-up procedures as needed. If warranted, the caseload manager notes any planned on-site activity, and the proposed date of the target examination and notifies the Director of Examination and Scheduler of the recommendation. The appropriate federal regulatory authority is also contacted and made aware of the Division's concerns and plan of action. This process ensures that emerging issues and adverse trends are brought to the attention of the appropriate individuals in a timely manner so that a safe and sound financial industry can be maintained.

In summary, the strength and resilience of Colorado's banking industry allows for risk-focused examination procedures to be utilized in general, as well as fewer enforcement actions. These factors have allowed the Division to maintain its examination schedule despite a reduction in staff and a steady increase in the asset base of banks. Should a decline in the overall financial condition of the industry occur, it would dramatically increase needed examination hours and enforcement actions, which would in turn, severely strain staff resources.

Operations Unit

The operations unit is responsible for applications, automation, examination scheduling, program development, training, internal audit and review, organizational policies and procedures, oversight of administrative staff, and enforcement of the Public Deposit Protection Act (PDPA). This unit is responsible for all administrative support to the Division. It manages the Division's $3.6 million budget including expenditure and revenue monitoring; the Division's accounting, procurement, travel, and vendor activities; completion of annual budget distribution; completion of all fiscal year closing requirements; and, funding need forecasts. In addition, the operations unit maintains the Division's database, electronic and other documents, and manages user support of all Division systems, including *Genesys*, *Alert*, and *ED*.

Another important function of the operations unit is to annually prepare a Fee Schedule for Board approval and to conduct semi-annual assessments of banks and trust companies. It ensures that annual PDPA assessments are completed and recovers expenditures for the previous fiscal year. The operations unit also manages the Division's formal training program, and answers telephone calls from financial institutions and the public for the purpose of exchanging information and solving problems, errors, and complaints.

PDPA Administration Unit

The PDPA unit is charged with monitoring compliance with the Public Deposit Protection Act, as well as bank examination scheduling. The PDPA (§ 11-10.5-101, *et. seq.,* C.R.S.) was enacted to protect uninsured State and local government funds held on deposit in Colorado banks. In the event eligible banks become insolvent, Colorado law provides for the expedited repayment of public deposits not covered by FDIC insurance. The Division of Banking, as Administrator of the PDPA, protects over $2 billion in state and local government deposits.

The Division of Banking currently regulates 219 state and nationally chartered banks for compliance with the PDPA. All collateral is pledged and released through the Colorado Division of Banking. Banks are required to report all public deposit accounts to the Division of Banking monthly. Based on data from those reports, an automated system calculates each bank's collateral requirements and notifies PDPA staff of any undercollateralized institutions. Division staff then contact the bank to ensure that additional collateral is quickly pledged. Division examiners travel on-site to the banks periodically to verify the accuracy of the public deposit reports that the banks prepare and send to the Division. Table 10 depicts PDPA exams for the preceding five fiscal years.

Table 10
PDPA exams, FY 97-98 to FY 01-02

Type of Institution	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Banks*	51	33	56	35	47
Industrial Banks	0	0	0	2	0
National Banks	18	24	24	18	21
Total	**69**	**57**	**80**	**55**	**68**

PDPA examinations of state-chartered banks are conducted during the course of the regular safety and soundness examinations of those institutions. The national bank PDPA examinations are conducted on a stand-alone basis.

A performance audit by the State Auditor in 2000 suggested that improved oversight would strengthen the protection of public funds. The Auditor noted that "the Division could enhance its examination procedures by increasing the frequency of targeted PDPA reviews in banks with high concentrations of public funds, even if they are classified as low-risk institutions" (p. 12). For the period under review, we note that the level of examinations in fiscal year 01-02 was approximately the same (68) as in fiscal year 97-98 (69), and fifteen percent less than the high of 80 in fiscal year 99-00.

According to the Division, the Banking Board's Policy 80-1, entitled "Risk-Based Examination Scheduling" was revised in response to the Auditor's concerns. The purpose was to increase the frequency of target public deposit examinations of well-rated banks with high concentrations of public deposits to once every 12 months. Banks with "high concentrations of public deposits" were defined in the policy as those with total public deposits in excess of 10 percent of the aggregate public deposits in all eligible public depositories. On November 6, 2000, November 12, 2001, and November 4, 2002, annual target public deposit examinations were conducted on the only bank in Colorado that held public deposits in excess of 10 percent of the aggregate public deposits in all eligible public depositories (Wells Fargo Bank West, N.A.). As of March 31, 2003, U.S. Bank, N.A., of Cleveland moved into the 10 percent and above category. Consequently, a targeted PDPA examination of U.S. Bank, N.A., Cincinnati began June 16, 2003, and was recently completed. Because so few banks in Colorado hold high concentrations of public deposits, increasing the frequency of those banks' PDPA examinations has not caused a significant increase in the number of PDPA examinations conducted each fiscal year.

In addition to examinations, the PDPA unit is responsible for examination scheduling. Bank examination scheduling involves: (a) determining which of the regulated institutions must be examined in a given fiscal year and when those examinations will be conducted; (b) meeting with the portfolio managers to initially plan and staff those examinations; (c) meeting with federal agency staff to plan and staff joint examinations; (d) notifying the institutions of the planned examinations; and, (e) publishing a weekly examination schedule, including examiner assignments, six to eight weeks in advance of the examinations.

Applications and Complaints

The major task assigned to the applications function of this unit is to review and analyze the complex financial, managerial, operational, and structural information/conditions related to applications submitted to the Colorado Division of Banking for a new bank charter (commercial bank, industrial bank, trust company, or foreign capital depository), license (money order company or money transmitter), merger, consolidation, change of control, and others. The unit must determine if the applicant has met all of the individual application requirements, develop the agency's position regarding the applicant's request, and prepare and present written and oral recommendations (including agency justification of recommendation) to the Colorado State Banking Board within required timelines. In addition, the applications segment of this unit is responsible for the management of application processes, including reviewing the necessary scope of background investigations, updating and improving all application forms, tracking certain application processing costs, making application forms and related information available on the Division's web site, and an ongoing assessment of new interagency application forms.

The major function of the complaints segment of this unit is to review and analyze written complaints against institutions regulated by the Division. This segment must determine whether there have been violations of law or rule. In addition, it acts as an arbitrator between complainants and regulated institutions when appropriate to find a resolution acceptable to both parties. The complaints segment is also responsible for the management of complaint processing, including updating and improving complaint information available on the Division's web site, as well as the revision, development, or deletion of policies related to complaint processing. Table 11 depicts consumer complaints for the preceding five fiscal years.

Table 11
Consumer Complaints, FY 97-98 to FY 01-02

Number of Complaints	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Bank	*	44	42	32	34
Industrial Bank	*	6	2	3	2
Trust Company	*	28	61	25	21
Total	*****	**78**	**105**	**60**	**57**

*The Division did not maintain detailed consumer complaint tracking sheets until FY 98/99. Prior to that time, complaints were simply tallied and reported to the Banking Board on a monthly basis.

One measure of the effectiveness of the Division's complaint process is to estimate the amount of money returned or saved by the average consumer. Table 12 depicts dollars saved by type of institution for the preceding five fiscal years.

Table 12
Consumer Dollars Saved, FY 97-98 to FY 01-02

Dollars Saved*	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Commercial Bank	N/A	$34,837	$14,404	$74,912	$58,490
Industrial Bank	N/A	$2,586	$2,087	$9,375	$0
Trust Company	N/A	$48,340	$15,074	$1,843	$42,305
Total	**N/A**	**$85,763**	**$31,565**	**$86,130**	**$100,795**

*Amounts reflect consumer funds saved through reimbursement of fees charged, transactions reversed, fraud losses recouped, trust company trading errors, and other settlements.

Consumers with complaints against institutions regulated by the Division are asked to provide the complaint in writing, with as much detail as possible. A referral letter, with a copy of the complaint, is forwarded to the institution with a requested response date. Upon receipt of a response, a Division staff member reviews the issues and responds to the complainant, with a copy to the regulated institution, explaining the findings and the resolution of the complaint.

The vast majority of cases involve poor communication, misunderstandings of loan or deposit contracts, and fee agreements. Very few complaints involve violations of law or regulation. The Division does not have the authority to adjudicate complaints involving matters of contract law or court proceedings. The Division's complaint manager resolves the majority of consumer complaints through discussion, negotiation, and moral suasion.

What is missing from this scenario is a procedure by which the bank itself, as a client of the Division, could lodge a complaint with the Division, especially concerning a particular examination, rating, or examiner. Examination appeal procedures exist at the federal level. We address this shortcoming in Recommendation 3. Table 13 depicts enforcement actions for the preceding five fiscal years.

Table 13
Enforcement Actions

	Type of Action					
Period	**BR**	**MOU**	**C&D**	**W/A**	**Close**	**Total**
FY 97-98	2	1	0	0	0	**3**
FY 98-99	0	1	1	0	1	**3**
FY 99-00	3	1	0	0	0	**4**
FY 00-01	5	1	0	1	0	**7**
FY 01-02	1	3	1	0	0	**5**
Total	**11**	**7**	**2**	**1**	**1**	**22**

Legend for Table 13 (listed in order of severity)
BR Board Resolution
MOU Memorandum of Understanding
C&D Cease and Desist Order
W/A Written Agreement – A federal enforcement action initiated by FRB w/Division part
Close Receivership - BestBank placed in receivership 7/23/98

Most of the reported actions were entered into jointly with the applicable federal regulatory authority.

The majority of Division and federal agency enforcement actions are based on "safety and soundness" concerns, that is, poor earnings, impaired capital, and/or asset quality weaknesses. The industry, buoyed by the strong economy, has posted very strong earnings over the last decade. The strong industry condition is evidenced by the fact that in recent years, over 90 percent of Division regulated banks, industrial banks, and trust companies have been rated a CAMELS "1" or "2." There is a general presumption that enforcement actions are not warranted at "1" or "2" rated banks (if examination findings warrant corrective action a more adverse rating would be assigned). It therefore follows that a limited number of enforcement actions would be initiated during this period. Nevertheless, many of the examination reports disclosed minor weaknesses and/or areas for improvement. These items were addressed by recommendations and written directives contained within the examination reports and transmittal letters.

Division enforcement actions are designed to achieve one or more of the following objectives: 1) Improve the financial condition of the institution; 2) Eliminate an unsafe or unsound condition (including violations of law or regulation); 3) Remove or suspend an individual from the institution and industry; and/or, 4) Correct the behavior of an institution-affiliated party. The enforcement recommendation process, standards, and procedures are detailed in Division Policy 70-1.

In general, the Banking Board acts to meet the following four objectives: (1) Improve the financial condition of an institution; (2) Eliminate an unsafe or unsound condition; (3) Remove or suspend an individual from an institution; and, (4) Correct the behavior of an institution-affiliated party. These objectives are not mutually exclusive. Enforcement actions may be taken to meet any, or all of these objectives.

The various types of actions and triggering criteria are outlined next.

The Division has both *formal* and *informal* enforcement tools to aid it in carrying out its supervisory and enforcement responsibilities when addressing violations of law, rule, regulation, condition imposed in writing, or written agreement entered into with the agency, as well as any unsafe or unsound practice. These tools range from informal actions such as advice and moral suasion to formal actions such as cease-and-desist orders. Informal enforcement actions generally require the agreement and cooperation of financial institution owners and management to be effective, and put the board of directors and management on notice in case a formal action may be necessary later. Formal enforcement actions may be consensual but usually are imposed upon financial institution owners and management by the regulators. Formal actions require administrative procedures prior to becoming effective and are subject to appeal to the Colorado courts.

Informal actions are generally used in institutions with composite ratings of “1” or “2,” and “3” with strong management. At a minimum it is Division policy that institutions with a composite rating of “4” or “5” for the latest safety and soundness, trust or information technology examinations are presumed to warrant formal enforcement action unless the Commissioner or designee documents that their problems are satisfactorily corrected or in the process of full correction. The severity of action chosen is based primarily on the institution’s current condition with consideration given to the cooperation, responsiveness, and capability of the board of directors and management.

The more frequently used enforcement actions listed in increasing order of severity are:

Informal Enforcement Actions

Board Resolutions (BR). A declaration by an institution’s board of directors outlining a plan to deal with the institution’s problems as identified by the regulators. The resolution sets forth reforms and time frames. This action is used when it is determined that the institution is not in serious jeopardy of failure and that the institution’s board and management are cooperating with supervisory officials. It is not a binding legal document.

Memorandum of Understanding (MOU). An agreement drafted by supervisory officials and signed individually by each member of the board of directors of the affected institution. It outlines specific actions the institution must take and establishes deadlines for reaching those goals. MOUs are generally used when it is determined that management and the board of directors of the institution have been adequately informed of the multiple deficiencies and in good faith will move toward elimination of the problems. It is not a binding legal document.

Formal Enforcement Actions

Cease and Desist Order (C&D). Requires a halt to illegal, unsafe, or unsound activities. An order may also require affirmative corrective action. C&Ds are issued either with the consent of the party named in the order or after the conclusion of a hearing, initiated by the Banking Board, serving notice of charges on the institution or individual. The issuance of a C&D is pursued if there is reason to believe an unsafe or unsound situation exists that could threaten the integrity or viability of an institution. C&D Orders are publicly disclosed and generate adverse publicity for the institution.

Removal or Suspension of Management Personnel. The Banking Board has the power to suspend or remove individuals from associating with a state chartered institution for specific violations of law, regulation, or agreement. Removal results in financial institution officers and directors being prohibited from further participation in the affairs of the institution and may be extended to other persons who may not hold an office or serve as a director. Grounds for removal are as follows:

- The person has: (1) violated the Banking Code, or any regulation of the Banking Code, or final C&D; (2) engaged or participated in any unsafe or unsound practice; (3) committed or engaged in any act, omission, or practice that constitutes a breach of such party's fiduciary duty; or (4) found guilty of certain civil or criminal offenses enumerated in section 11-102-303(8), C.R.S.; and,

- The financial institution has: (1) suffered or will suffer substantial financial loss or damage; (2) the interests of the institution's depositors could be seriously prejudiced as a result; (3) the person has received financial gain by reason of his/her bad actions; or, (4) the violation, unsafe or unsound practice, or breach of fiduciary duty, involves personal dishonesty or demonstrates a willful or continuing disregard for the safety or soundness of the institution.

Civil Money Penalties. Civil money penalties may be assessed against financial institutions, their service corporations, or subsidiaries for certain statutorily defined actions. Assessment of a civil money penalty provides a strong deterrent to violations of laws, regulations and orders as well as breaches of fiduciary duties and unsafe or unsound practices.

Civil money penalties may be assessed by the Banking Board against any person who has violated any final cease and desist order. Alternatively, civil money penalties may be assessed against any financial institution or any executive officer, director, employee, agent or other person participating in the conduct of the affairs of the institution who violates or knowingly permits another person to violate the Banking Code or a Banking Board rule or who engages or participates in any unsafe or unsound practice.

When assessing a civil money penalty, consideration is given to the size of financial resources and good faith of the person, institution or company being assessed, the gravity of the violation, and the history of previous violations.

Civil money penalties under the Banking Code can only be assessed if the Banking Board determines that penalties were not imposed on the individual or institution by another governmental authority. Moreover, Colorado law limits the amount of penalty at $1,000 per day. Federal banking laws allow much higher levels of civil money penalties to be assessed. These restrictions effectively negate civil money penalties as an enforcement tool for the Division. In nearly any circumstance warranting civil money penalties, the Division would defer to the federal banking regulator because of the higher cap.

Analysis and Recommendations

During the course of this sunset review, the Department of Regulatory Agencies (DORA) solicited input from a variety of sources. A number of significant issues were presented and considered including:

- The efficiency and effectiveness of the U.S. dual banking system as it applies to Colorado;
- Consolidation of the Colorado Division of Banking and the Colorado Division of Financial Services; and,
- The importance of adequate, flexible funding and staffing.

Some of these issues are discussed in the recommendations that follow. Those that are not discussed, or not discussed in detail, were found to have fallen outside the scope of the statutory criteria that govern sunset reviews.

Recommendation 1 – Continue the Division of Banking until 2013.

The mission of the Colorado Division of Banking (Division) is to serve and protect the public interest by promoting a safe and sound financial institutions industry through continuous quality regulation and supervision. More specifically, the Division is responsible for public deposit protection and the regulation of state-chartered commercial banks, industrial banks, trust companies, money transmitters, and money-order companies. The Division holds charter and license application hearings and issues rules and regulations affecting regulated institutions. Division staff conduct examinations of state-chartered institutions and licensees and examine the following functions in financial institutions: Public Deposit Protection Act compliance, trust departments, electronic funds transfer, electronic data processing, and Uniform Consumer Credit Code compliance. The Division also works closely with the Federal Reserve Bank and the Federal Deposit Insurance Corporation concerning the regulation of commercial and industrial banks, and certain federally mandated insured trust companies.

All banks accepting deposits from the public must obtain a national or state bank charter before they can open for business. The basic purpose of chartering is to assure that institutions accepting funds from the public are competent and deserving of the public's trust. The Division of Banking is the state agency that ensures a safe and sound banking industry in Colorado by means of its state bank chartering procedures, bank examinations, enforcement actions, and other regulatory activities. It also constitutes one half of the dual banking system discussed earlier in this report. It is the current policy of the General Assembly to preserve and promote a dual federal and state banking system (§ 11-101-102, C.R.S.). Consequently, the Division of Banking should be continued until 2013 given that by means of its oversight of the banking industry, the Division serves a fundamental role in maintaining a healthy Colorado economy.

Should the Colorado Division of Banking and the Colorado Division of Financial Services be Consolidated into One Agency?

Statutory evaluation criteria direct DORA to assess "if regulation is necessary, whether the existing statutes and regulations establish the least restrictive form of regulation consistent with the public interest, considering other available regulatory mechanisms and whether agency rules enhance the public interest and are within the scope of legislative intent" (§ 24-34-104(9)(b)(II), C.R.S.). Given the similarity of functions performed by the Colorado Division of Banking and the Colorado Division of Financial Services, the question arises whether these two state regulatory bodies can be combined into one agency so as reduce costs and realize efficiency gains. The Division of Banking primarily regulates banks, while the Division of Financial Services regulates credit unions. Both banks and credit unions have the option of obtaining either a national or a state charter.

Proponents of consolidation argue that combining Colorado's Division of Banking and Colorado's Division of Financial Services would result in a more efficient agency, which may lead to more cost-effective regulation. One estimate is that consolidation would result in annual savings of $120,000. This analysis is based on the elimination of one Commissioner and the administrative staff support for that Commissioner.

Opponents of consolidation argue that it is unreasonable and difficult for one Commissioner to assume the duties of another full-time position without some adverse impact on his or her duties. It is more likely that additional staff would be required to handle delegated duties, and this may erode any cost savings realized by consolidating posts. Furthermore, each Division as currently structured, has its distinct constituency which is used to established practices that may or may not be aligned across Divisions. Opponents also point out that both Divisions are self-funded by industry assessments, consequently the perceived or actual combining of funds would raise fundamental questions of equity.

Given the modest cost savings, reorganization costs, and regulatory confusion that may arise, we conclude that consolidation of the Colorado Division of Banking and the Colorado Division of Financial Services is neither feasible, nor desirable at this time.

Recommendation 2 – Reduce the size of the Banking Board by one member and alter its composition to make it non-partisan.

Section 11-102-103, C.R.S., creates the Banking Board (Board). The required composition of this body is as follows:

- Four members who are executive officers of state banks with at least five years of practical experience;
- One member who is an executive officer of an industrial bank;
- One member who is an executive officer of a trust company; and,
- Two members who have experience in finance and serve as public members.

Of the eight members, not more than four can be of the same major political party. At all times, at least one member must reside west of the continental divide. Members are appointed by the Governor with the consent of a majority of the Senate. The term of office for each member is four years. Four members of the Board constitute a quorum, and action taken by a majority of those present at any meeting at which a quorum is present represents official Board action.

Partisan politics do not play any part in Board deliberations and actions. Furthermore, the Banking Board is highly professional and deals mostly with technical matters specific to banking. However, an eight-member board is an artificial byproduct of having two major political parties, and is not consistent with the size of most state boards. For example, at the Department of Regulatory Agencies, the State Board of Accountancy, the Board of Real Estate Appraisers, and the State Board of Veterinary Medicine all have seven members. We recommend therefore that the statutory provision that the Board be comprised of not more than four members from the same major political party be repealed, and that the size of the Board be reduced to seven members.

Alternatively, the General Assembly might wish to consider whether increasing the size of the Banking Board to nine members is a more desirable public policy option. In a national study of boards and commissions the average size of boards was found to be nine members. The study concluded that the interests considered by a board expand when there are more members, but may also slow the pace of decision making.[7]

Recommendation 3 – Institute an independent appeal process regarding "Material Supervisory Determinations," define this term to include bank examinations, and establish by rule criteria to govern appeals to the Board.

In reviewing the complaint procedures of the Division of Banking, and as a result of our discussions with federal officials, it came to our attention that the Division does not currently have an independent appeals process in place to satisfy any concerns that state chartered banks might have regarding mandatory state examinations or other supervisory actions. It bears repeating that the composite ratings that banks receive following an examination help to determine their viability as ongoing business concerns, as well as the assessments they pay to the Division. Consequently, enhancing the fairness and effectiveness of this aspect of regulation is important. The fundamental purpose of such an appeals process is to increase the integrity of regulation and to provide an opportunity for correction when an appeal is successful.

At the federal level, bank regulators have implemented an intra-agency appellate process. We modeled this recommendation on the federal guidelines.

[7] Mitchell, Jerry (1997). "Representation in Government Boards and Commissions". *Public Administration Review*, Vol .57, no. 2, p. 165.

Section 309(a) of the Riegle Community Development and Regulatory Improvement Act of 1994 (Pub. L. 103-325, 108 Stat. 2160) (Act) requires the FDIC, as well as the other federal banking agencies and the National Credit Union Administration Board, to establish an independent intra-agency appellate process to review material supervisory determinations. The Act defines the term “independent appellate process" to mean a review by an agency official who does not directly or indirectly report to the agency official who made the material supervisory determination under review. In establishing the appeals process, the FDIC must ensure that any appeal of a material supervisory determination by an insured depository institution is heard and decided expeditiously, and that appropriate safeguards exist for protecting the appellant from retaliation by agency examiners.

The Act requires the FDIC to establish an appeals process to review material supervisory determinations. The term ”material supervisory determinations” is defined in the Act to include determinations relating to: (1) examination ratings; (2) the adequacy of loan loss reserve provisions; and, (3) loan classifications on loans that are significant to an institution. The Act specifically excludes from the definition of ``material supervisory determinations'' a decision to appoint a conservator or receiver for an insured depository institution or to take prompt corrective action pursuant to section 38 of the Federal Deposit Insurance Act, 12 U.S.C. 1831o.

We worked with the Colorado Banking Commissioner to adapt and apply these guidelines to Colorado banks under the Division’s jurisdiction. The results follow in the form of proposed statutory language:

> (1) THE BOARD SHALL ESTABLISH BY RULE AN INDEPENDENT APPELLATE PROCESS TO ADDRESS ADVERSE MATERIAL SUPERVISORY DETERMINATIONS AFFECTING STATE CHARTERED BANKS. FOR PURPOSES OF THIS SUBSECTION (1) MATERIAL SUPERVISORY DETERMINATIONS ARE DEFINED AS:
> (A) EXAMINATION RATINGS, INCLUDING COMPOSITE SCORES, INFORMATION TECHNOLOGY, AND TRUST DEPARTMENT RATINGS;
> **(**B) DETERMINATIONS RELATING TO THE ADEQUACY OF LOAN LOSS RESERVE PROVISIONS;
> (C) DISPUTED ASSET CLASSIFICATIONS EXCEEDING TEN PERCENT OF TOTAL CAPITAL;
> (D) DETERMINATIONS RELATING TO VIOLATIONS OF LAW OR REGULATION; AND,
> (E) OTHER DETERMINATIONS THAT MAY HAVE AN EFFECT ON AN INSTITUTION'S CAPITAL, EARNINGS, OPERATING FLEXIBILITY, ITS CAPITAL CATEGORY FOR PROMPT CORRECTIVE ACTION PURPOSES, OR OTHERWISE AFFECT THE NATURE AND LEVEL OF SUPERVISORY OVERSIGHT ACCORDED THE INSTITUTION.
>
> (2) IN PROMULGATING THE RULE PROVIDED FOR IN SUBSECTION (1) THE BOARD SHALL APPLY THE FOLLOWING CRITERIA, CONSIDERATIONS, AND POLICIES:

(A) THE INITIAL APPEAL SHALL BE HEARD BY A PERSON OR PERSONS SELECTED BY THE BOARD WHO DID NOT PARTICIPATE IN, OR REPORT TO, THE PERSONS WHO MADE THE MATERIAL SUPERVISORY DETERMINATION UNDER REVIEW;
(B) THE BOARD SHALL ESTABLISH SAFEGUARDS TO PROTECT BANKS THAT FILE APPEALS FROM RETALIATION;
(C) ALL APPEALS MUST BE IN WRITING AND APPROVED BY THE APPELLANT'S GOVERNING PRINCIPAL OR A MAJORITY OF PRINCIPALS ON FORMS APPROVED BY THE BOARD;
(D) ALL APPEALS MUST BE HEARD WITHIN 90 DAYS AND DECIDED WITHIN 180 DAYS;
(E) THE BOARD SHALL CLASSIFY THE INSTITUTIONS ELIGIBLE TO APPEAL;
(F) THE BOARD SHALL ENCOURAGE INFORMAL RESOLUTION PROCEDURES;
(G) THE BOARD SHALL ENCOURAGE COORDINATION WITH OTHER STATE AND FEDERAL REGULATORY AUTHORITIES; AND,
(H) THE BOARD SHALL MODEL THE RULE PROVIDED FOR IN SUBSECTION (1) ON RELEVANT FEDERAL GUIDELINES TO THE EXTENT THAT FEDERAL GUIDELINES ARE CONSISTENT WITH THIS SECTION.

(3) NOTWITSTANDING ANY PROVISION OF THIS SECTION, AN APPEAL OF AN ADVERSE MATERIAL SUPERVISORY DETERMINATION WILL NOT AFFECT, DELAY, OR IMPEDE ANY FORMAL OR INFORMAL SUPERVISORY OR ENFORCEMENT ACTION IN PROGRESS.

In conclusion, this recommendation will enhance the integrity of bank regulation in Colorado. Moreover, allowing state chartered banks to appeal adverse material supervisory determinations will make state bank charters more competitive in relation to national charters and inject additional fairness into the existing regulatory scheme.

Recommendation 4 – Authorize the Bank Commissioner to examine any relevant relationship between state banks, affiliates, and third-parties.

In 1998, during a joint federal/state examination of a problem bank, restricted access to a third party's financial information impeded the bank examination process. According to the Material Loss Review of *BestBank* (a public document), *Century*, a third-party provider, exercised substantial control over *BestBank's* credit card programs. The FDIC made the determination, however, that it lacked statutory authority to examine *Century*. When the FDIC finally gained access to *Century's* data processor in June 1998, the examiners determined that "past due" credit card accounts had not been reported accurately. *Century's* control was significant considering that the *BestBank/Century* subprime credit card receivables represented 71 percent of the bank's total assets as of May 29, 1998. In addition, *Century* did not have the financial capability to indemnify the bank for losses associated with the related credit card programs.

Clearly, it is important to have access to financial information from third-party and affiliate entities that exercise significant control over an insured institution's loan portfolio, particularly when the institution is relying on the service provider to indemnify the bank for any losses in the loan portfolio and to provide information to the bank regarding the status of the portfolio. Without this third-party access, bank examiners cannot accurately determine the insured institution's true financial condition and potential risk to the industry. *BestBank's* failure cost the FDIC insurance fund over $200 million.

Section 10(c) of the Federal Deposit Insurance Act provides in part

> . . . in making any examination under paragraph (2) or (3), any examiner appointed under paragraph (1) shall have power, on behalf of the Corporation, to make such examinations of the affairs of any affiliate of any depository institution as may be necessary to disclose fully --
>
> (i) the relationship between such depository institution and any such affiliate; and
>
> (ii) the effect of such relationship on the depository institution.

By way of comparison, Colorado's Banking Code holds that "the commissioner, if he or she deems it necessary or if required by the banking board, may examine the books and records of the controlling shareholder of a state bank and any affiliated entities of the controlling shareholder for the purpose of determining the safety and soundness of the state bank" (§ 11-102-301(3)(a), C.R.S.) Further, for purposes of this provision, "affiliated entity" or "affiliate" means an entity in control of a controlling shareholder (§ 11-102-301(3)(f)(I), C.R.S.).

In sum, to avert a future problem concerning access to financial information from third parties and to clarify the existing provisions of the Banking Code, the following statutory changes should be made: section 11-102-301(3)(a), C.R.S., "the commissioner, if he deems it necessary or if required by the banking board, may examine the books and records of the controlling shareholder of a state bank and any affiliated entities of the controlling shareholder AND ANY RELATIONSHIP AMONG THEM for the purpose of determining the safety and soundness of the state bank." Furthermore, the definition of "affiliated entity" or "affiliate" should be amended to mean "an entity in control of a controlling shareholder or AN ENTITY CONTROLLED BY A CONTROLLING SHAREHOLDER" (§ 11-102-301(3)(f)(I), C.R.S.).

Recommendation 5 – Amend section 11-105-101, C.R.S., to clarify that more than one loan production office is permitted.

In May 1995, the General Assembly adopted House Bill 1355 to make conforming amendments to Colorado law in relation to the Riegle-Neal Interstate Banking and Efficiency Act of 1994. This federal law lifted the limitation on the number of permissible bank branches. However, loan production office limitations were not changed at that time in the Colorado Banking Code.

The best means by which to achieve the policy objectives of the Riegle-Neal Interstate Banking and Efficiency Act of 1994, as well as enhance the competitiveness of Colorado banks that wish to do business in neighboring states is to amend section 11-105-101(1), C.R.S., to read:

> Any bank, upon application to and approval by the banking board, may operate one OR MORE loan production officeS as defined by the banking board.

In short, this is a necessary housekeeping change to the Banking Code to make it consistent with federal law.

Recommendation 6 - Make section 11-105-401(1)(d), C.R.S., of the Banking Code consistent with the Financial Institutions Reform, Recovery and Enforcement Act of 1989.

The failure during the 1980s of many financial institutions, especially savings and loans associations, subjected the real estate industry and appraisers to increased federal oversight. Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989, as amended, as well as federal regulations led to the use of state certified or licensed real estate appraisers to perform federally related transactions. Under FIRREA either a state-certified or licensed appraiser must be used for all real estate-related transactions of $250,000 or more. Currently Colorado law sets this amount at $100,000. To make Colorado's Banking Code conforming to FIRREA, as well as to account for appreciation in property values, the $250,0000 threshold should be incorporated into Section 11-105-401(1)(d), C.R.S., as follows:

> The property shall be entered on the books at not more than cost or fair market value, whichever is less, except as otherwise provided by the banking board. Each bank maintaining property acquired to satisfy indebtedness will obtain an initial written appraisal and subsequent appraisals as to fair market value by a qualified independent appraiser or such other person as the banking board may approve. Such subsequent appraisals shall be obtained pursuant to rules and regulations of the state banking board; except that, for purposes of this paragraph (d), an appraisal, as defined in section 12-61-702 (1), C.R.S., by an appraiser certified, licensed, or registered pursuant to section 12-61-708, C.R.S., shall not be required on properties initially valued pursuant to this paragraph (d) at ~~one hundred~~ TWO HUNDRED AND FIFTY thousand dollars or less. If such appraiser or other person approved by the banking board certifies in writing such appraiser's or other person's opinion that the fair market value has not declined, this opinion may be substituted for a subsequent appraisal.

In short, this is a necessary housekeeping change to the Banking Code to make it consistent with federal law.

Recommendation 7 – Repeal the Colorado Investment Deposit Act.

The Colorado Investment Deposit Act became effective May 31, 1990. The purpose of this legislation was to promote economic development through investment in small businesses by providing tax exemptions on savings and investments. The legislative declaration set out in section 11-37-101, C.R.S., provides in part:

> . . . in light of existing economic conditions in Colorado, measures need to be taken to encourage, promote, and stimulate economic development in Colorado, that existing federal and state income tax laws discourage persons from making long-term investments and from setting aside savings which would otherwise be available for financing the creation and growth of Colorado business enterprises. . .

The original policy objective was to stimulate economic growth by exempting Colorado income tax on interest income earned on Colorado investment deposits issued by eligible banks. In theory, the banks could increase deposits and lower funding costs by offering slightly lower rates on the investment deposits because of the tax benefit (as is the case with municipal bonds). The bank in turn was required to make best efforts to lend at least 50 percent of the funds to small businesses with priority given to minority-owned and women-owned businesses. In practice, however, the tax incentive proved inadequate to stimulate deposits.

The interest income earned on a certificate of deposit issued pursuant to the provisions of the article by a qualified financial institution is exempt from Colorado income tax. Colorado's effective income tax rate is approximately 1.4 percent. This tax exemption does not provide a strong incentive for investors, nor does it provide sufficient incentive to permit financial institutions to offer slightly lower certificate of deposit rates to recoup the cost of record keeping and reporting as mandated by law. The Colorado Investment Deposit Act requires institutions to maintain detailed records and to report their activities annually to the State Bank Commissioner or the State Commissioner of Financial Services. The Commissioners are in turn required to compile the information and provide a summary report to the Department of Revenue. The administrative burden on eligible institutions results in limited participation. Since 1996 only two banks have reported accepting investment deposits, and as of December 31, 2002, the total amount of money involved in the program was approximately $300,000 in the form of outstanding loans. Despite low bank participation, the Division of Banking is required to send out annual reminders and forms to all state banks, industrial banks, and national banks. The mailing triggers a flood of phone calls from bank staff that are not aware of the provisions of this law. In addition, bankers are concerned with what they perceive to be an ambiguous standard for determining compliance.

In short, the administrative burden placed on banks and the Division has increased regulation without meeting the original public policy objectives of the Colorado Investment Deposit Act. Consequently, we recommend that Article 37 of Title 11 of the Colorado Revised Statutes be repealed.

Recommendation 8 – (Administrative) – The Division should create and implement a comprehensive recruitment, selection, retention, training, and cross-training strategy to address its bank examiner shortage.

One of the most important issues facing the Division of Banking is adequate staffing. Recruiting and retaining qualified staff to operate the examination unit is a continuing challenge according to the Director of Examinations. The examination of banks is the core function of the Division. A number of retirements over the past several years has reduced the number of Division bank examiners, who unfortunately also depart with considerable institutional knowledge and memory. Moreover, the increase in the number of *de novo* banks has increased the workload for the current bank examiners without a corresponding increase in authorized FTEs. The Division has been fortunate in that the FDIC and Federal Reserve Bank have been able to assist on mandated bank examinations.

Moreover, due to the specialized nature of the work bank examiners take approximately three to five years to become fully proficient, especially when an individual has had no prior regulatory experience. Even experienced examination staff require training to stay current with changes in laws and regulations, as well as industry changes that affect the safety and soundness of banks. Given the existing bank examiner shortages, however, training is not given the emphasis that it deserves.

It is also important to report that Division staff informed us that even though two bank examiner positions are currently vacant, no recruitment efforts are underway to fill these positions because budgetary shortfalls preclude any hiring. The Division had 28 authorized examiner/auditor positions and five vacancies as of July 1, 1999. During this time, the Division had 28 postings and filled 19 positions, but had 16 positions vacated for a net gain of 3. As of June 30, 2003, 26 of the 28 authorized positions were filled. Budget constraints and projected retirement payouts preclude filling the two vacant positions at this time. This is the main reason why we opted to document this problem by way of this administrative recommendation instead of requesting additional FTE authorization. In this light, our recommendation to eliminate the mandatory examination of money transmitters gains added importance given that the central purpose of that recommendation is to make available up to 1.00 FTE to perform bank examinations. Money transmitter examiners have a general knowledge of bank safety and soundness examinations, and could with an investment in training, be fully competent to perform bank examinations. Bank examinations are the core function of the Division of Banking, and its primary mission is to ensure a safe and sound banking industry in Colorado.

It is central to our argument that this recommendation be considered as a companion recommendation to Recommendation 2 in the 2003 Sunset Review of the Money Order Act.

In conclusion, the Division of Banking should create and implement a comprehensive recruitment, selection, retention, training, and cross-training strategy to address its bank examiner shortage.

Appendix A – Sunset Statutory Evaluation Criteria

(I) Whether regulation by the agency is necessary to protect the public health, safety and welfare; whether the conditions which led to the initial regulation have changed; and whether other conditions have arisen which would warrant more, less or the same degree of regulation;

(II) If regulation is necessary, whether the existing statutes and regulations establish the least restrictive form of regulation consistent with the public interest, considering other available regulatory mechanisms and whether agency rules enhance the public interest and are within the scope of legislative intent;

(III) Whether the agency operates in the public interest and whether its operation is impeded or enhanced by existing statutes, rules, procedures and practices and any other circumstances, including budgetary, resource and personnel matters;

(IV) Whether an analysis of agency operations indicates that the agency performs its statutory duties efficiently and effectively;

(V) Whether the composition of the agency's board or commission adequately represents the public interest and whether the agency encourages public participation in its decisions rather than participation only by the people it regulates;

(VI) The economic impact of regulation and, if national economic information is not available, whether the agency stimulates or restricts competition;

(VII) Whether complaint, investigation and disciplinary procedures adequately protect the public and whether final dispositions of complaints are in the public interest or self-serving to the profession;

(VIII) Whether the scope of practice of the regulated occupation contributes to the optimum utilization of personnel and whether entry requirements encourage affirmative action;

(IX) Whether administrative and statutory changes are necessary to improve agency operations to enhance the public interest.

Appendix B – Comparison Matrix of Old and Recodified Banking Code

House Bill 03-1257

by Representative Marshall and Senator Lamborn

A bill for an act

Concerning a nonsubstantive recodification of Colorado's banking laws.

New Banking Code

Article 101 General Provisions
- Part 1 Short Title & Policy
- Part 2 Effect on Existing Banks
- Part 3 Application
- Part 4 Definitions

Article 102 Division of Banking
- Part 1 Commissioner & Banking Board
- Part 2 Proceedings
- Part 3 Records, Reporting & Information
- Part 4 Assessments & Fees
- Part 5 Conflicts of Interest, Penalties, Removal, Suspension, & Enforcement

Article 103 Organization & Corporate Functions
- Part 1 General Corporate Powers
- Part 2 Capital Requirements
- Part 3 Chartering a State Bank
- Part 4 Shares & Distributions
- Part 5 Directors & Officers
- Part 6 Indemnification & Insurance
- Part 7 Merger, Consolidation, Conversion, & Sale of Assets
- Part 8 Liquidation, Dissolution, & Reorganization

Article 104 Holding Companies
- Part 1 Holding Companies Generally
- Part 2 Acquisition of Control of Banks & Bank Holding Companies

Article 105 Banking Practices
- Part 1 General Provisions
- Part 2 Electronic Funds Transfers
- Part 3 Reserves, Loans, & Investments
- Part 4 Property, Sales, Borrowing, & Signature Guaranty
- Part 5 Safe Deposit & Safekeeping Facilities
- Part 6 Financial Institutions, Operation of Branches, Organizational and Operational Equality

Article 106 Fiduciary Business

Article 107 Criminal Offenses

Article 108 Industrial Banks
- Part 1 General Provisions
- Part 2 Powers
- Part 3 Charters
- Part 4 Records, Reporting, & Information
- Part 5 Directors, Penalties, Removal, Suspension, & Enforcement
- Part 6 Liquidation & Dissolution
- Part 7 Banking Practices
- Part 8 Criminal Offenses & Violations

Article 109 Trust Companies
- Part 1 General Provisions
- Part 2 Powers
- Part 3 Charters
- Part 4 Records, Reporting, & Information
- Part 5 Directors
- Part 6 Offenses, Penalties, Removal, Suspension, & Enforcement
- Part 7 Liquidation, Dissolution, & Emergency Charters
- Part 8 Appeals
- Part 9 Trust Practices

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Side-by-Side Comparison Chart

Old Provisions	New Provisions
11-1-101. Short title.	11-101-101
11-1-101.5. Declaration of policy.	11-101-102
11-1-102. Definitions.	11-101-401
11-1-103. Effect on existing banks.	11-101-201
11-1-104. Terms of first officials appointed.	Repealed.
11-1-105. Application of code.	11-101-301
11-1-106. No private right of action.	11-101-302
11-2-101. Division of banking - creation - subject to termination - repeal of article.	11-102-101
11-2-102. Banking board.	11-102-103
11-2-103. Powers of banking board.	11-102-104
11-2-103.5. Roles and authority of banking board and commissioner - review of powers and duties.	11-102-105
11-2-103.6. Hearing officers - powers - procedure - order final.	11-102-201
11-2-104. Subpoenas - witnesses - production of records.	11-102-202
11-2-104.5. Effect of good faith reliance on orders, rules, or regulations of banking board.	11-102-203
11-2-105. Court review.	11-102-204
11-2-106. Powers of commissioner.	11-102-102
11-2-107. Banking board and commissioner - exercise of powers.	11-102-105
11-2-108. Examinations and examiner's reports.	11-102-301

11-2-109. Bank reports to banking board - requirements for acquiring control.	11-102-302 11-102-303
11-2-110. Commissioner's annual report - publications.	11-102-304
11-2-111. Records.	11-102-305
11-2-111.5. Information confidential.	11-102-306
11-2-112. Access to records.	11-102-307
11-2-113. Bank records - preservation - reproduction.	11-102-308
11-2-114. Assessments.	11-102-401
11-2-114.1. Administrative fees.	11-102-402
11-2-114.5. Division of banking cash fund - creation.	11-102-403
11-2-115. Banking interests of officers and employees.	11-102-501
11-2-116. Exemption from liability - when.	11-102-502
11-2-117. Assessment of civil money penalties by banking board.	11-102-503
11-2-118. No indemnification or insurance against civil money penalties.	11-102-504
11-2-119. Removal of director, officer, or other person.	11-102-505
11-2-120. Suspension of director, officer, or other person.	11-102-506
11-2-121. Informal enforcement authority.	11-102-507
11-2-122. Statements derogatory to state banks - penalty.	11-102-508
11-3-101. General corporate powers.	11-103-101
11-3-102. Trust, fiduciary, and agency powers - when.	11-103-102

11-3-103. Capital.	11-103-201
11-3-104. Inadequacy of capital - assessments.	11-103-202
11-3-105. Liability of shareholders.	11-103-203
11-3-106. Incorporators.	11-103-301
11-3-107. Application fees.	11-103-302
11-3-108. Organization expenses. (Repealed)	N/A
11-3-109. Application for charter.	11-103-303
11-3-110. Procedure for granting or denying charter.	11-103-304
11-3-111. Subscription calls.	11-103-401
11-3-112. First meetings of stockholders - director's oath - bylaws.	11-103-402
11-3-113. Stockholders' meetings - voting trusts - preemptive right - transfer of stock.	11-103-403
11-3-114. Directors and officers.	11-103-501
11-3-115. Directors' meetings - duties.	11-103-502
11-3-116. Waiver of notice - meeting or vote.	11-103-404 11-103-503
11-3-117. Amendment of articles - change of location - authorized but unissued stock.	11-103-405
11-3-118. Dividends - when.	11-103-406
11-3-119. Undivided profits account. (Repealed)	N/A
11-3-120. Director and officer insurance and fidelity bonds - legislative declaration.	11-103-601
11-3-121. Indemnification and personal liability of directors, officers, employees, and agents.	11-103-602

11-3-122. Deposit insurance - membership in federal reserve system - federal national mortgage association.	11-103-603
11-3-123. Emergency branch facility converted to a state bank. (Repealed)	N/A
11-4-101. Definitions.	11-101-401
11-4-102. Merger or conversion.	11-103-701
11-4-103. Approval of merger by directors.	11-103-702
11-4-104. Approval by banking board.	11-103-703
11-4-105. Approval by stockholders - rights of dissenters.	11-103-704
11-4-106. Effective date of merger - certificate.	11-103-705
11-4-107. Continuation of corporate entity.	11-103-706
11-4-108. Conversion from state bank to national and vice versa.	11-103-707
11-4-109. Nonconforming assets.	11-103-708
11-4-110. Sale of all assets of bank or department.	11-103-709
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