Amalgamation of the Southern California Banking Industry: San Diego a Microcosm

Cheryl R. Lee
Thomas M. Cooley Law School

Follow this and additional works at: http://scholarlycommons.law.cwsl.edu/cwlr

Recommended Citation
Available at: http://scholarlycommons.law.cwsl.edu/cwlr/vol35/iss1/3

This Article is brought to you for free and open access by CWSL Scholarly Commons. It has been accepted for inclusion in California Western Law Review by an authorized administrator of CWSL Scholarly Commons. For more information, please contact alm@cwsl.edu.
AMALGAMATION OF THE SOUTHERN CALIFORNIA BANKING INDUSTRY: SAN DIEGO A MICRO COSM

CHERYL R. LEE

I. Introduction .................................................................................................................................. 42
II. Historical Context .................................................................................................................... 44
III. The Impact of Federal Regulatory Controls and California State Regulations on San Diego Amalgamation Activity ................................................................. 48
IV. Why Financial Institution Managers & Directors Chose Amalgamation to Promote Growth ............................................................................................................................. 79
V. The Growth of Financial Institutions Through Amalgamation ........................................... 82
VI. San Diego Financial Institutions in 1985 ............................................................................... 83
VII. How Amalgamation Affected the San Diego Community, Financial Institution Customers, and Employees ................................................................. 95
VIII. The Current San Diego Financial Market .......................................................................... 131
IX. Conclusion and Recommendations ...................................................................................... 143

APPENDIX A SAN DIEGO MERGER TIME LINE—1986 to 1998 ........................................... 151
APPENDIX B CLOSING AND ASSISTANCE TRANSACTIONS IN SAN DIEGO COUNTY 1985-1996 .............................................................. 157

*Assistant Professor of Law, Thomas M. Cooley Law School, Lansing, Michigan. Assistant Corporate Counsel, Great American Bank, San Diego, California, 1985-90. Professor Lee participated in several mergers, acquisitions and corporate finance debt offerings and borrowings in the forum of a federal savings and loan which later converted to a publicly-held California stock savings institution, sold its retail branch system to Wells Fargo, and was taken over by the Office of Thrift Supervision in 1991. The author wishes to thank Samantha Stevins, Julie Clements, Judith Bernstein, and Geoffrey Bohm.
I. INTRODUCTION

In the wake of the April 13, 1998, announcement of a mega-merger between BankAmerica and NationsBank, creating the first ever coast to coast banking organization, it is essential to examine how these merger and acquisition deals will affect bank customers. San Diego, almost BankAmerica’s hometown, is a stark illustration of this national trend. This deal alone will affect over twenty-nine million bank customers in twenty-two states; merger mania has the potential to affect over 140 million depositors and customers nationally.

Since the financial regulatory changes of the 1980s, especially deregulation and interstate banking, financial institutions have used mergers and acquisitions as their primary method of growth. While the amalgamation option has been tremendously successful for banking organizations, it has been perilous for bank customers. The national and super-regional financial institutions, no longer in a position where they have to please all the depositors all the time, have reduced services to the individual customer, instituted higher fees for services offered, reduced support to the communities in which they do business, and there are less opportunities for small business credit. Since the merger frenzy began, the sheer number of financial institutions a depositor has vying for their business has been significantly reduced. The disappearance of banking organizations in San Diego was a preview of what was to happen nationally.

In 1985, there were 14,417 insured commercial banks and 3,626 insured savings institutions doing business in the United States. At the industry’s largest point there were 30,000 commercial banks in the United States. Of the insured savings institutions, 219 were located in California. By 1996, 9,530 insured commercial banks and 1,924 insured savings institutions remained, and only sixty-six of those insured savings institutions continued to do business in California. “Troubles for California banking gained national prominence when Security Pacific’s position continually weakened in its ‘equal merger’ with BankAmerica. This merger with its shifting equilibrium also foreshadowed the changing fortunes of [northern and southern Califor-
When 1987 came to a close, there were thirty-seven banking organizations in the San Diego financial market. Sixteen of those organizations were considered major players.

More than any other single factor, amalgamation has been responsible for this result. From the beginning of San Diego's first merger activity in 1981 by Great American Bank, to the August 1997 merger between Great Western and Washington Mutual, leaving Washington Mutual with combined assets of $94 billion, and the latest development to affect San Diego, the BankAmerica/NationsBank merger that will create a $600 billion bank, the growth of financial institutions in Southern California, San Diego particularly, has been achieved through amalgamation. The amalgamation of banking has had a huge impact on the San Diego bank customer, the well-being of the community, local unemployment, and the city's economic growth.

Historically, banking was limited geographically. Today, primarily because of the Riegle-Neal Act of 1994 and the heightened competition amalgamation has brought, the public perceives banking to be fragmented, overly saturated, and even inefficient. The public fear of large banks having too much power is still very prevalent in society. So much power in the hands of so few is against the public interest. This is the kind of fear that led to today's restrictive banking environment. For example, constraints remain an integral part of the new interstate legislation, such as the limit on the percent of deposits that a single bank can control in any one state or nationally under Riegle-Neal.

By 1992, mergers and acquisitions had left San Diego with ten major banking organizations. Today the San Diego market is serviced by only three large commercial banks and five small, mainly local institutions which of-
fer some savings products but mainly promote themselves as commercial organizations, emphasizing their commercial products.\textsuperscript{14} If not for the local credit unions, the institutional savings market would be extinct.

All of this is contrary to the public interest. What remains available today for San Diego depositors are banking organizations that are huge conglomerates or tiny establishments. The continuing trend with super-regional and national banking organizations not only compromises competition but threatens to eliminate it. Whether service to customers and the communities into which these financial institutions venture remains any part of the business of banking is, as a consequence, a growing concern. It is not necessary for financial institutions to sacrifice customer service, community involvement, and limit credit opportunities to maximize profits.

\section*{II. Historical Context}

"The first public announcement of the organization of a savings bank in the United States appears in the \textit{Christian Disciple} of Boston in 1816. The Society for the Prevention of Pauperism had conducted an inquiry into philanthropic methods of encouraging and protecting the savings of the poor."\textsuperscript{15} The result of the inquiry was a small donation of capital and the bank was open for business.\textsuperscript{16} Inspired by the clergy, banking was created for the people.

These savings institutions\textsuperscript{17} were originally established for charitable purposes and not necessarily to make a profit. The original task of banking was to encourage people to deposit money in savings accounts, facilitate home ownership, and supply credit to groups of workers or farmers who could not obtain adequate credit at existing banking facilities.\textsuperscript{18} "Commercial banks were . . . criticized for neglecting the financial needs of farmers, artisans, and small traders, as well as low- and middle-income people, especially with regard to their needs for mortgage loans to finance the acquisitions of houses. Specialized thrift deposit institutions, ranging from various

\textsuperscript{14} Grossmont Bank, Bank of Commerce, Peninsula Bank, Scripps Bank, and First National Bank complete the San Diego market of financial institutions.

\textsuperscript{15} \textsc{Morris L. Ernst}, \textit{Too Big} (1940).

\textsuperscript{16} See id.

\textsuperscript{17} For purposes of discussion in this paper, the term "savings institutions" encompasses savings banks, thrifts, savings and loan associations, mutual savings banks, and is defined as a savings organization established to make loans for the purchase of real estate or a home to those persons who hold accounts at the organization and the public in general from the deposits of such account holders. Such institutions are either chartered by the state in which an organization does business or the federal government, and is insured by the Federal Savings and Loan Association or the Federal Deposit Insurance Corporation. If chartered by the federal government, a savings institution is designated as a federal savings and loan association (S&L), and is regulated by various financial regulatory agencies, including but not limited to the Federal Home Loan Bank System.

\textsuperscript{18} See \textsc{Reforming Financial Systems}, \textit{supra} note 4, at 142, 144, 149.
types of savings banks and credit cooperatives to credit unions and housing finance institutions, were created or emerged spontaneously to fill these gaps in the financial system throughout the late eighteenth and nineteenth centuries."

"Savings banks originally invested all their funds in government bonds," so it was only natural they would become regulated by the government. "By 1875 the investment choice for savings banks had been enlarged to include bonds of railroad and utility companies, and first mortgages up to about half of the value of [the pledged] real estate . . . . With billions invested in real estate, these banks became vital instruments" in the growth and development of cities. Certainly this was true in the case of San Diego. Two of the city's most predominant savings institutions, Great American Bank beginning in 1885 and Home Federal Savings and Loan beginning in 1934, were undeniably instrumental in building the city of San Diego.

During World War II the Roosevelt Administration introduced a plan to coordinate national housing policies. Central to this approach was stimulating a sense of cooperation between all federal agencies overseeing both banks and savings institutions. Commercial banks\(^1\) had traditionally been insured by the Federal Deposit Insurance Corporation (FDIC), and were regulated by the Federal Reserve Board (FRB or "Board") and the Comptroller of the Currency. Savings institutions received federally subsidized loans, were under the regulatory control of the Federal Home Loan Bank Board (FHLBB or "Bank Board"), and secured insurance protection from the Federal Savings and Loan Insurance Corporation (FSLIC).

"As a result of the Great Depression, Congress created a federal insurance-of-accounts system to restore public confidence in the security of thrift institutions and to ensure a sound and economical means of home financing. The FSLIC fund reimburses a thrift depositor for savings lost through the failure of a savings and loan association. It [was] however, the statutory duty of the [Federal Reserve] Board to administer the FSLIC fund\(^2\) under the Federal Home Loan Bank Act of 1932 and the National Housing Act of 1934.\(^3\) "FSLIC insurance, in the case of state-chartered associations, is voluntary and becomes effective only if such institutions apply for it and are accepted. As a condition for eligibility under the program, state-chartered

19. Id. at 13.
21. Id.
23. For purposes of discussion in this paper, a "commercial bank" is a corporation which receives money on deposit, makes loans, issues promissory notes, cashes checks or drafts and discounts commercial paper, is either a state chartered organization or a federally chartered national bank, and is regulated by various financial regulatory agencies, including but not limited to the Comptroller of the Currency.
thrifts agree to inspection and regulation by the Board. The Board... possesses the ultimate authority to terminate an association's insurance if it finds that institution engaging in unsafe and unsound practices.\(^2\) The majority of state-chartered California savings institutions did in fact apply for FSLIC insurance when they converted from federal or mutual savings organizations to stock organizations incorporated in the state of California.

"By 1940, [there were] about six hundred [mutual savings] organizations [across the country], controlling about ten billion dollars of the nation’s savings, collected from about twelve million separate accounts."\(^{26}\) "[T]otal deposits in ordinary commercial banks [on the other hand], amount[ed] to more than forty billion dollars."\(^{27}\) Just as it is today, “a depositor who [did] not like the way ‘his’ bank was run had but one [ultimate] remedy—withdrawal of his moneys from deposit.”\(^{28}\)

In 1942, Congress created the National Housing Agency and placed under its jurisdiction the Federal Home Loan Bank Board; in 1955 the Bank Board became the premier independent federal savings institutions regulatory agency.

Over the next twenty years savings institutions marketed and provided only one major product, home mortgage loans. The task of commercial banks by contrast, was to satisfy the short-term credit needs of consumers and businesses. The remaining banking services (stock market and bond sales) became the domain of investment banks that were regulated by the Securities and Exchange Commission.

Since the beginning of World War II, banking has been extremely lucrative in Southern California. From the 1930s to the early 1960s, savings institutions primarily, and banks to a lesser degree, were the actuators of the American dream of home ownership. Savings institutions profited by making more interest on the home mortgages they offered than they paid on savings accounts. Commercial banks and savings institutions continued to focus on offering different services and different accommodations to customers. The two rarely competed for deposits from the same customers. "The National Bank Act,\(^{29}\) as well as state banking laws, limited banks to three types of ‘business of banking’ powers in order to protect the safety and soundness of the banking system: deposit taking, credit granting, and credit exchange.”\(^{30}\)

"The Banking Act of 1933 prohibited the payment of interest on checking accounts, and the Federal Reserve Board's Regulation Q placed a ceiling on the interest rates banks and thrifts could pay on time and savings ac-

\(^{25}\) Id. at 454.

\(^{26}\) ERNST, supra note 15, at 97.

\(^{27}\) Id.

\(^{28}\) Id. at 98.


\(^{30}\) Tart, supra note 12, at 925.
counts." Regulation Q, which had long been considered a banker's tool because it discouraged competition, now caused difficulties for banking organizations. This regulation, which previously restricted only commercial banks, was imposed on savings institutions in 1966. Regulation Q had provided savings institutions with the ability to pay one-quarter to one-half of a percentage point more than commercial banks on deposits. This advantage was perceived as compensating S&L customers for the limitation on banking products that savings institutions could offer. Now, for the first time commercial banks and savings institutions were on equal footing in attracting depositors, although Congress did empower S&Ls to continue offering a slightly higher fraction of a percentage point on deposits than commercial banks. It was in this way that the savings institutions' deposit business stabilized.

"In the years of generally stable rates, home loans had been a low risk investment. Repayment was all but assured. Even when strapped, borrowers kept up with mortgage payments. But home loans presented a high risk indeed when rates were unstable. A [S&L] could not make money if it had to pay depositors ten cents on the dollar while earning only six cents in long term mortgages booked years earlier." In response to this squeeze, Congress in 1964 allowed [savings institutions] to venture out of real estate into college and other education loans. Eight years later, in a step that put [savings institutions] in head-to-head competition with commercial banks, Massachusetts thrifts used a loophole in the banking laws to introduce an interest-bearing checking account called a negotiable order of withdrawal (NOW) account in an effort to attract short term funds. Although customers were restricted to a few withdrawals a month from the account, the service proved so popular that Congress approved the accounts nationwide in 1980.

By 1988 savings institutions not only regularly offered NOW accounts, but also made consumer loans and commercial loans. These developments, much more than others, warned savings institutions that they must in the years ahead compete with commercial and even investment institutions for depositors. Products, priceability, interest rate return, and services in general would be key to the future success of both banks and savings institutions. Around 1980, S&Ls began to lobby Congress heavily for new regulations that would allow them to offer a greater array of products yielding more profitable short-term investments. In 1986, under

31. JONATHAN R. MACEY & GEOFFREY P. MILLER, BANKING LAW AND REGULATION 30 (2d ed. 1997) [hereinafter MACEY & MILLER].
35. Id. at 57-58.
36. See id.
both savings association laws and the regulations of the FHLBB governing federal associations, savings institutions were permitted to invest up to 40% of their assets in nonresidential real estate loans. After which came the slew of federal laws concerning deregulation, which led directly to a surge of merger and acquisition activity.

Although amalgamation has been the basis of growth for American banking throughout modern history, deregulation in the 1980s was the catalyst for catastrophic changes in Southern California banking. Emergence and growth of the major commercial banks and the local savings institutions in the San Diego market occurred almost exclusively through mergers with smaller banks and multiple branch acquisitions. For example, during 1981 and 1982, San Diego-based Great American Bank completed the merger and acquisition of eight small regional savings and loan associations. It increased the S&L’s net worth by $46.1 million, which was the “combined net worth of these eight associations at their respective dates of merger.”

Those initial eight mergers set the stage for Great American’s phenomenal growth to an asset size of $13 billion in 1986, gained in large part through mergers and acquisitions.

III. THE IMPACT OF FEDERAL REGULATORY CONTROLS AND CALIFORNIA STATE REGULATIONS ON SAN DIEGO AMALGAMATION ACTIVITY

Both federal and state law provided an environment conducive to bank merger activity in San Diego’s financial industry. Typically, states today limit mergers by reviewing “the need for banking... facilities in the proposed community; the ability of the community to support the proposed bank...; the previous banking history of the community; opportunities for profitable use of bank funds as indicated by the average demand for credit; the number of potential depositors; the volume of bank transactions; the stability, diversity, and size of the businesses and industries of the community...;” and the character, reputation, business experience, motives, financial standing and responsibility of the organizers, incorporators, proposed officers, stockholders and directors. Certainly this is criteria the California State Banking Department uses. However, the federal and California financial regulatory agency perspective was to deregulate, so all of the above criteria was evaluated from a pro-deregulatory point of view. During the mid-1980s when deregulation in a number of industries became America’s economic decree, the banking industry was no exception. But by 1990 deregu-

38. See GREAT AMERICAN FIRST SAVINGS BANK, 1986 ANNUAL REPORT 35 (1987), See also GREAT AMERICAN FIRST SAVINGS BANK, OFFERING CIRCULAR = 15,000,000,000 5.0% COLLATERIZED EUROyen NOTES DUE 1992, Mar. 25, 1987, at 17 [hereinafter GREAT AMERICAN OFFERING CIRCULAR].
lation had helped create the S&L failures and subsequent bailout that was expected to cost at least $200 billion.40

Unlike the deregulation that occurred in the transportation industry, the focus for savings institutions and banks was not on balancing the interests of communities and banking customers for the purpose of economic efficiency. Instead, the objective was to create a minimally supervised banking environment, and to increase profitability. It was through deregulation that the federal government granted financial institutions a multitude of new investment powers as part of the Direct Investment Rule.41

Federal and California law during the 1980s permitted the development of new financial instruments, which were used to aggrandize bank assets and liabilities. Often banking institutions and their officers had no previous expertise with these instruments. In addition, federal law had no regulatory standards meant to deal specifically with the impervious procedures to be implemented in connection with these new and risky financial tools. Also, on the federal level, "net worth requirements were effectively eliminated, allowing weak S&Ls to grow rapidly using insured deposits."42 Then in 1989, the Financial Institution Reform, Recovery and Enforcement Act (FIRREA)43 enabled Savings Association Insurance Fund (SAIF)44 insured "thrift institutions to change their charter to become commercial banks."45

FIRREA wreaked havoc because it totally changed the administration of savings institutions. These new charters did nothing to change the administrative problems that had occurred under FSLIC's guidance.

As a result of favorable state regulation, California was one of the regions where the largest losses occurred. California law was more favorable for savings institutions than for commercial banks, so there was far less to give incentive for national commercial banks to be incorporated in California. Accordingly, Wells Fargo Bank, like many other California banking organizations, changed the company's state of incorporation from California to Delaware in February 1987.46

"The typical [S&L] failure was a stockholder-owned, state-chartered institution in Texas or California where regulation and supervision were most lax (although major failures also occurred at federally chartered S&Ls, at mutuals, and in many other states). The failed institution typically had experienced a change of control and was tightly held, dominated by an individual

44. Id. § 1821(a)(6).
45. STATISTICS ON BANKING, supra note 3, at A-1.
with substantial conflicts of interest... one who used the institution's capital to support personal business ventures. The typical [commercial bank failure was a large bank which] had grown at an extremely rapid rate, achieving high concentrations of assets in risky ventures such as acquisition, development, and construction (ADC) loans and/or direct investments of various kinds."

The California legislature played a huge role in liberalizing the state regulatory environment in favor of S&Ls. For instance, Assembly Bill 3539, passed by the California legislature in 1982, completely removed restrictions on California-chartered savings institutions to invest their assets in real estate and other non-conventional investments. These investments were of course made with federally insured deposits. Eventually, however, many of the California-chartered savings institutions returned to federal charters. As a result, the California Department of Savings and Loan suffered large assessment fee losses and many of the large S&Ls, like Great American and Home Federal who had active Political Action Committees and had heavily contributed to the campaigns of candidates seeking state office, decreased their support. S&L failures in San Diego, at least in the case of Great American and Home Federal, typically occurred because of these issues.

By 1980 the savings industry was corpse-like.

The first liquidation and payout of a thrift in ten years occurred in 1981. During that ten year period failed S&Ls had been merged into stronger S&Ls and accounts transferred, but now depositors of the failed savings institutions lined up around the block to get whatever part of their money they could. In that same year the deposit insurance fund had resources of $8.5 billion to back savings institutions which had deposits of $600 to $700 billion. The numbers used to describe the size of the problem were staggering. It was clear FSLIC had to stem the drain or risk big budget outlays.

The Reagan Administration, in its desperation to keep savings institutions open, directed FSLIC to use FSLIC notes, forbearance, or anything that did not swell the deficit to avoid dealing with insolvencies by closing these S&Ls and paying depositors. There would be no direct bailout, at least not yet.

Federal law mandated the closing of insolvent savings institutions, but there was a loophole. FSLIC had authority to assist troubled institutions or to sell or merge them if doing so was cheaper than closing them and paying off depositors. Paying depositors was usually costlier than a merger in the short run, but it often proved least costly once a S&L’s assets were sold to help offset the government’s initial cash outlay to depositors. FSLIC sold strug-
gling institutions to almost all who expressed interest: healthy buyers, other S&Ls, commercial banks, and nonbanking companies.

"Federal law generally prohibits nonbanking businesses from owning commercial banks . . . the rationale being that general commerce should be separated from banking in order to prevent conflicts of interest," but these same businesses can own a S&L. "Traditionally the Bank Board imposed regulations that mimicked the policy applying to commercial banks, thus barring retailers from owning S&Ls. [However in 1981] the Bank Board waived these regulations, as it was empowered to, without congressional approval." Initially, federal regulations precluded commercial banks, but not savings institutions, from interacting in the investment banking market. Later, savings institutions were also prohibited from such activities by both state and federal regulations, although federal regulators again had the power to withdraw such regulations without congressional consent. Federal law also prohibited commercial banks from crossing state lines without permission from the state they were entering. To limit competition, over the years local bankers made sure their state legislators barred outsiders. Originally, this law did not apply to savings institutions but S&L regulators traditionally had elected to impose similar geographic limits.

FHLBB had the power to remove all federal law restrictions for purchasers of troubled S&Ls, and it did so often. The Bank Board eliminated still other ailing thrifts through mergers that clumped together several sick institutions in the hope that a single, healthier institution would emerge. Though such a strategy threatened to make one larger problem out of several smaller ones, the Bank Board thought the gamble worth taking. Mergers avoided depositor payouts and slowed the rate at which dollars were being sucked from the FSLIC's dwindling reserves. During a two year period, 1,000 savings institutions disappeared in this way. "Many were . . . bought privately without government aid. But a large chunk, nearly half, were transferred to new owners with the assistance of the Bank Board." These were the type of activities which San Diego based Great American First Savings Bank and Home Federal Savings & Loan participated in to win the Bank Board's approval of their own merger activity. One of the eight initial mergers Great American completed and several of its subsequent acquisitions and mergers were effected with the assistance of FHLBB and FSLIC. In these various ways, amalgamation emerged as the tool to avoid depositor payouts, slow the demise of FSLIC, and to restore the savings industry.

52. Id. at 95.
53. Id. at 96.
54. Id.
There are five justifications for regulating financial firms:

1. **The Preservation of Solvency**: The primary function of financial regulation is to protect [depositors]... on the grounds that well-advised members of the public would want such protestations... The most common regulatory tools used to preserve solvency are minimum capital requirements, portfolio restrictions and diversification requirements, [imposing] general standards of conduct on firms and their employees, and periodic reporting requirements supplemented with on-site examinations... Additional tools include regulatory review... to establish new financial firms or acquire controlling interests in existing firms... In evaluating such applications, regulatory authorities typically consider the integrity and experience of management, their business plans for the entity, and... competitive conditions in the markets they propose to enter.

2. **Prevent Systemic Economic Disruptions**: A distinct goal of financial regulation is to prevent bank failures that could spread costs through the economic system by sparking financial panics, disrupting the payments system or interfering with the credit underwriting process.... Certain government programs, such as central bank liquidity authority and regulation of the payment systems, are designed to insulate an economy from the negative externalities associated with financial-institution failure.

3. **Prevent Uncompetitive Practices**: A separate reason to regulate financial enterprises is to safeguard competition in credit and capital markets... These justifications proceed from an assumption that without special supplemental regulation, financial firms would gain sufficient market power to extract excess profit, or to deny credit to, disfavoured borrowers.... The premise is that financial firms could enjoy special public subsidies that, without legal constraints, might be shared with affiliated or otherwise favoured borrowers. Concern over anti-competitive practices of this sort partially explain why financial intermediaries are often prohibited from making direct investment to other business enterprises and are also strictly regulated in providing credit to, or engaging in transactions with affiliated entities.

4. **Redistributive Norms**: Financial firms are also often regulated to advance redistributive norms. For example, most systems of insurance regulation prohibit firms from charging different rates on the basis of certain classification, such as race or wealth, even if those distinctions would be actuarially fair.... Common mechanisms for advancing redistributive norms are mandatory terms for dealing with borrowers and creditors or requirements regarding the allocation of assets.

5. **Political Economy**: Finally, some legal systems use financial regulation to realize political goals. These include rules limiting foreign ownership of domestic firms or restrictions on the geographic expansion of urban banks into rural communities.

Every one of the major federal regulations passed from 1985 to 1997 was created because of, or contain some elements of, each of these five justifications. These elements, along with certain regulatory changes, created opportunities for bank holding companies, commercial banks, and savings institutions, but also increased competition among them.

Various restrictions have been imposed both nationally and by the state of California, which affect the remaining three major San Diego commercial banking organizations, BankAmerica, Wells Fargo Bank, and Union Bank. The traditional tools to expand, such as lending limits, the type and amount of investments, opening branch offices, acquiring other banks and savings institutions, and engaging in the underwriting of certain securities are all subject to regulation and examination by the Comptroller of the Currency, the FDIC, OTS, and the Board of Governors of the Federal Reserve.

Major regulatory changes affecting these three San Diego commercial banks have been implemented in the past few years and continue to incite changes in financial institutions as the industry progresses. Primarily, it has been deregulation that encouraged the expansion of banking services and the powers of savings institutions to engage in broader commercial and consumer bank services. Deregulation also permitted the sale of investment products by banking organizations and even eliminated interest rate controls on deposits, while generally reframing the distinctions between commercial banking organizations and savings institutions. Geographic restrictions on commercial banks and savings institutions will also continue to disappear as a result of the Riegle Neal Act.56

Let’s explore these regulatory changes and their effect one by one.

1. The Banking Act of 1933 Which Includes the Glass-Steagall Act and the Federal Deposit Insurance Act

a. The Glass-Steagall Act

The underlying weaknesses, mainly the diseconomies of scale and lack of asset diversification of small banks in the banking industry between 1929 and 1933, caused the stock market crash of 1929, the ensuing depression, and the resulting bank failures of the early 1930s,57 essentially the complete collapse of the banking system. The response of Congress was to pass the Banking Act of 1933, also called the Glass-Steagall Act,58 which is a fundamental piece of legislation that remains the centerpiece of American Banking policy.59
Glass-Steagall had five provisions:

1. In response to the political charges that the Depression had been caused by bank speculation in securities, the Act separated commercial banking from investment banking.

2. The Act prohibited the payment of interest on checking accounts and permitted regulation of interest paid on time and savings deposits. This was an attempt to reduce the cost of funds for banks by suppressing competition for deposits.

3. The Act regulated bank holding companies at the federal level by requiring multibank holding companies to obtain Federal Reserve approval before they could vote the stock of subsidiary banks, if any subsidiary bank was a member of the Federal Reserve System.

4. Glass-Steagall also amended the McFadden Act (which restricted national banks to branch only within their home cities even in states where state-chartered institutions had broader branching privileges) and permitted expansion of the branching privileges of national banks.

5. Finally, the Act established a program of federal deposit insurance.

The Competitive Equality Banking Act of 1987 (CEBA), which altered the impact of Glass-Steagall and the Bank Holding Company Act, had more of an effect in California than it did nationally. CEBA temporarily blocked banks from expanding into real estate, securities, and some insurance activities. “Prior to CEBA, section 408 of the National Housing Act prohibited savings and loan holding companies from owning thrifts in more than one state. Shortly after CEBA was passed the Federal Reserve Board proposed that bank holding companies regulated under BHCA, be permitted to acquire healthy savings and loans insured by FSLIC.” In addition, “the acquisition of a ‘bank’ is governed exclusively by section 3 of the BHCA, which contains the Douglas Amendment’s prohibition on interstate banking.” CEBA encouraged California banks positioning themselves to merge and acquire other banking organizations to form bank holding companies of their own.

b. The Federal Deposit Insurance Act

The purpose of the Federal Deposit Insurance Act (FDIC) is “to promote through regulation a safe and stable system of affordable housing fi-
FDIC was designed "to improve the supervision of savings associations; to curtail investments and any other activities of savings associations that pose unacceptable risks to FDIC funds; to promote the independence of the FDIC from the institutions whose deposits it insures; to increase the surety of FDIC funds; to establish both the Resolution Trust Corporation to contain, manage, and resolve failed savings associations (the FDIC provides funds from public and private sources to accomplish this purpose) and an Office of Thrift Supervision under the general oversight of the Secretary of the Treasury; to strengthen the enforcement powers of federal regulators of depository institutions; and to strengthen the civil sanctions and criminal penalties for defrauding or damaging depository institutions and their depositors."68

The FSLIC scandal increased the enforcement powers, expectations, and operation of this Act. After the demise of FSLIC and during the operations of the Resolution Trust Corporation and the creation of the Office of Thrift Supervision, the Federal Deposit Insurance Act was viewed as a law to regulate savings institutions more stringently. Provisions of this Act were strengthened and molded by several subsequent amendments enacted specifically to address banking matters concerning savings institutions, as well as to refine its historical relationship with commercial banks.

In 1990, the FDIC increased the insurance rate for deposits. The new rate, due to become effective on January 1, 1991, was projected to have a phenomenal effect on non-interest expenses of savings institutions for future years. Most savings institutions estimated a projected increase of millions just for 1991 alone; for example, in the case of San Diego Trust and Savings Bank the increase was over $1 million in 1991 in that expense category.69

FDIC deposit insurance and bank regulation continue to have an important role in creating a stable banking environment, which minimizes the risk to FDIC funds.

[Recently] most everything has gone well for banks and thrifts. There have been few failures, and earnings have achieved record levels, not only in absolute terms, but measured as a percentage of assets and capital. Bank performance has benefited from the combination of a growing economy, relatively stable prices and relatively stable interest rates. Apart from economic factors, ... institutional factors also are contributing to [safer banks] .... The experience of the [1980s] probably has made bankers more cautious about lending, concentrations and internal controls. Disclosure has improved. Bank analysts and large customers use output from bank reports, and the quality of data in those reports has improved, [partly because of] more cautious behavior by accounting firms. Capital requirements are now uniformly monitored and enforced so that banks are pushed to rectify shortfalls early. In addition, banks no longer have to compete with [those banking organizations] whose pricing reflects excessive lever-

67. *Id.*
68. *Id.*
age. Early [regulatory] intervention is also likely to force troubled banks to look for help while they still have positive value. High valuations . . . [make] it easier to find help. The failures and/or absorptions of so many [banking organizations] have lessened some excessive competition, although geographic expansion through branching and computer-based services may more than offset this reduction in competition. [Finally], most banks have had the opportunity to eliminate or write off longer-term, low-interest-rate loans and investments. 70

2. The Bank Merger Act (Section 1828 of the Federal Deposit Insurance Act)

The Sherman Antitrust Act, 71 designed to prevent monopolies in trade or commerce, and the Clayton Act, 72 conceived to prohibit transactions which would restrain trade, lessen competition, or create a monopoly, are also important components of antitrust banking law.

The Bank Merger Act (BMA) 73 prohibits mergers, consolidations, and purchases of assets with assumption of liabilities between banks and savings institutions unless the prior written approval of the appropriate bank regulatory agency has been obtained. Authority to administer the BMA is divided among several responsible agencies that are identified in the act. The Office of Thrift Supervision is responsible for mergers of federally insured savings institutions. 74 The FDIC is responsible for mergers, acquisitions, consolidations, or assumption transactions between federally insured and non-insured banks. 75 The Comptroller of the Currency handles transactions between insured national banks that are the acquiring bank, assuming bank, or resulting bank. 76 If a state member bank is the acquiring, assuming, or resulting bank, the Federal Reserve Board is the responsible agency; for a nonmember insured state bank, FDIC is responsible. 77

Before proscribing any action on a proposed transaction, the responsible agency is required to publish notices at certain intervals during the review process prior to granting any approval. The lead agency must also request and evaluate reports from any other responsible agency on the competitive aspects of the proposed transaction. Like the BHCA, a BMA analysis requires the responsible agency to consider the convenience and needs of the communities to be served, products and services currently available and offered via the proposed transaction, and the financial and managerial resources of the acquiring or resulting bank. If the proposed transaction would

70. FEDERAL DEPOSIT INSURANCE CORPORATION, HISTORY OF THE EIGHTIES: LESSONS FOR THE FUTURE, VOLUME II, SYMPOSIUM PROCEEDINGS 84 (Jan.16, 1997).
72. Id. § 12.
74. See id. § 1462(a).
75. See id. § 1828.
76. See id. § 1813.
77. See id. §§ 1828(c)(1), (2)(A)-(C).
create or tend to create a monopoly or substantially lessen competition without the justification of a "convenience and needs" rebuttal, then the responsible agency must deny approval. This is the same process which is followed under a BHCA procedure.

These BMA and BHCA regulatory provisions on federal merger law as applicable to financial institutions differ from general federal antitrust law. General antitrust law requires prior notification, but not prior regulatory approval for any of the proposed transactions described above. Therefore, these transactions require additional time, analysis, reporting, and expense for banking organizations than for companies outside of the banking arena. The BMA and BHCA require a thirty-day stay of the proposed transaction even after the appropriate regulatory agency tenders its approval. In addition, the financial regulatory agency regulations specifically impose a "public interest" analysis when an antitrust violation is alleged pursuant to financial regulations, whereas there is no specific "public interest" defense under general antitrust laws. In fact, some anti-competitive transactions are entirely permitted if the transaction could serve the "public interest" in some other equally important manner.

3. The Direct Investment Rule of 1987

The "Direct Investment Rule" was passed during the deregulation period by the FHlBB in 1987 under the authority of the National Housing Act of 1934 and the Federal Home Loan Bank Act. The National Housing Act was used as the regulatory tool to establish FSLIC for the purpose of administering a federal insurance scheme for savings institutions.

Direct investments were "investments in equity securities, real estate, service corporations, and operating subsidiaries." The Rule limited a savings institution's ability to make direct investments beyond a certain level without the prior approval of the Board. If a savings institution met its regulatory capital requirements and it had capital equal to or in excess of 6% of its total liabilities it was permitted to make direct investments up to three times its capital, or if the institution's total liabilities were below 6% and it still met its regulatory capital requirements, it was permitted to make direct investments up to 3% of its assets or 2.5 times capital, whichever was greater. In both situations, capital was to be calculated at the end of the month preceding the direct investment.

80. Id. § 1421.
81. See MACEY & MILLER, supra note 31, at 24.
83. See id. § 563.9-8(b)(2)(i)-(iii).
84. See id.
85. See id.
It was later the conclusion of the Bank Board that "direct investments posed greater risks to the financial health of thrifts than mortgage [lending] which was the traditional business of thrifts."66 This became apparent because of the large number of savings institutions that failed or were visited by financial difficulty throughout the 1980s, and the "unprecedented stress placed on the FSLIC fund"67 because of the number of savings institutions in this situation. The Bank Board "after investigation found a correlation between these emerging financial difficulties and the increasing trend of state-chartered [savings institutions] to purchase 'direct investments', [such as] a wide variety of commercial ventures, including equity securities and real estate."68 This was particularly true for savings institutions chartered in California, since "California regulations permitted unlimited direct investment without regard to risk."69

Time has proven that, among other regulatory innovations created in the 1980s to expand the power of savings institutions, the Direct Investment Rule was a significant contribution to the desire of both bank and savings institutions to explore mergers and acquisitions as a primary means of expansion and growth.

4. The Bank Holding Company Act of 1956

A bank holding company is "any company which has control over any bank or over any company that is or becomes a bank holding company."90 The requisite control is defined as: (1) owning, controlling, or having the power to vote 25% or more of voting securities of a bank; (2) the power to control the election of a majority of directors of a bank; or (3) where the Federal Reserve System Board of Governors determines the company controls the management or policies of a bank.91

Under the Bank Holding Company Act of 1956 (BHCA),92 a bank holding company generally cannot acquire or retain direct or indirect ownership or control of the voting shares of any company that is not a bank. A "bank," as defined in the BHCA, is (1) an institution insured under the Federal Deposit Insurance Act, or (2) one that accepts demanded deposits (any deposits the customer may withdraw by check or similar means) and is engaged in making commercial loans.93 The BHCA governs mergers, consolidations, or acquisitions of banks or bank holding companies by institutions

87. Id. at 450.
88. Id.
89. Id. at 452.
91. See id.
92. Id. § 1843 (a)-(c).
that are or will become bank holding companies. The Change in Bank Control Act governs acquisitions of commercial banks or thrifts by individuals or groups of individuals, and the Savings and Loan Holding Company Act governs these same transactions involving savings and loan holding companies. The acts all require the satisfaction of the Clayton and Sherman antitrust acts as a precondition to approval of the merger.

For example, when Wells Fargo & Company (the parent of Wells Fargo Bank) owns or acquires ownership of more than 5% of the voting stock of any company or bank or savings institution, the BHCA imposes certain restrictions on the company's activities. This has significant consequences on the operations of a banking organization. Wells Fargo & Company was the tenth largest bank holding company in the United States as of December 31, 1986. Its principal subsidiary is Wells Fargo Bank. Under the Bank Holding Company Act, Wells Fargo and any other bank holding company is required to regularly file reports of its operations with, and is subjected to examination by, the Federal Reserve Board.

As a result of mergers and acquisitions, many banking organizations become holding companies, subject to holding company regulation. Under federal law, the BHCA will define any company which owns another banking organization as a holding company. For example, Washington Mutual is a holding company because it owns three savings institutions, and has the right to elect to be treated by the Board as a savings bank holding company for purposes of the BHCA, if it so desires. The advantages of doing so could be salient to a banking organization. Such an election could be made to win regulatory approval for an amalgamation opportunity, to appear conciliatory in regulated supervisory transactions if the compliance with certain activities and investments is beneficial for a banking organization, or for the purpose of obtaining advances from the FHLB.

5. The Financial Institutions Supervisory Act of 1966

The Financial Institutions Supervisory Act was designed to broaden the regulatory and supervisory authority of federal agencies over insured banks and savings institutions. It amended the Home Owners Loan Act of 1933 by giving the FHLBB, the Comptroller of the Currency, and the FDIC the power to issue an order to cease and desist (after issuing a notice of...
service concerning the charges) through its own attorneys if it finds any rule, charter, law, or regulatory violation in connection with the granting of any application, request, or written agreement entered into with the Bank Board that would lead to any unsafe or unsound practices committed by a savings institution, a national bank, or a state member or nonmember insured bank. Specifications for cease and desist order proceedings, hearings and judicial review, the initiation of any temporary orders, subpoena power, penalties, and enforcement of such orders were addressed. The Supervisory Act also subjected directors and officers of an insured institution to cease and desist orders for their involvement in any unsafe or unsound practice of the institution constituting a violation of their fiduciary duties. Provisions for the removal of a director or officer from office and the appointment of a conservator or receiver were made.

The National Housing Act, section 407, and the Federal Deposit Insurance Act were amended by the Supervisory Act to allow for the voluntary or involuntary termination of insurance for insured savings institutions and banks. Provisions for the issuance of cease and desist orders, similar to those cited immediately above, were instituted. Finally, the FDIC and FSLIC maximum insurance limits on a insured deposit of any depositor was increased from $10,000 to $15,000 by the Supervisory Act of 1966.

6. The Depository Institutions Deregulation and Monetary Control Act of 1980—DIDMC

Congress found that limitations on interest rates payable by banks and savings institutions on deposits discouraged customers from saving money because these customers knew the market rate of return on their savings was limited by federal regulation. The Congressional concern was that these limitations created inequities for depositors, impeded the ability of depository institutions to compete for funds, and did not achieve their purpose of providing an even flow of funds for home mortgage lending. On March 31, 1980, DIDMC was enacted for the purpose of providing for the phase out and ultimate elimination (over a six year period) of the maximum rate of interest and dividend limitations which may be paid by depository institutions.

103. See id. § 1464(d).
104. See id.
105. See id.
106. Id. § 1818(a).
107. Termination under this amendment to the National Housing Act automatically constituted a removal of the institution from Federal Home Loan Bank membership.
109. See Financial Institutions Deregulation and Monetary Control § 121 (CCH 1980); see also Public Law 96-221 (1996).
Also under this Act, all depository institutions were required to maintain reserves on their transaction accounts and non-personal time deposits; NOW (negotiable order of withdrawal) accounts were nationally permitted; insurance limits on deposit accounts were increased to $100,000; and S&Ls were given the authority to invest up to 20% of their assets in consumer loans, commercial paper, and corporate debt securities. Savings institutions were relieved of the $75,000 lending limit on real estate mortgages and were permitted to lend up to 90% of the value of a home or more if the amount above 90% was covered by mortgage insurance. State usury laws on first mortgages by banks, S&Ls, credit unions, and mortgage banks were preempted, but the Act left a state with the ability to override this preemption if they acted legislatively within three years from DIDMC passage. The financial regulatory agencies were directed to simplify their regulations generally, especially the truth-in-lending regulations. All state imposed ceilings on business and agricultural loans over $25,000 and small business loans were also preempted by DIDMC. Last, DIDMC imposed on national banks changes in real estate holdings, preferred stock dividends, trust powers, holidays, appraisal rights and examinations, and imposed a moratorium on foreign acquisitions of United States depository institutions.

7. The Depository Institutions Act of 1982—Garn-St. Germain

Garn-St. Germain granted financial institutions the power to offer insured money market funds, eliminated the ability of a savings institution to pay slightly higher interest on time and savings accounts than could banks under Regulation Q, and authorized accounts with deregulated rates. Garn-St. Germain led to the total deregulation of interest rates throughout the financial industry. In San Diego this Act spurred banking organizations to begin offering a myriad of new investment products in their branch locations, including money market funds. This was the catalyst for banking organizations to begin cross-selling a variety of financial products to their existing customers. By allowing savings institutions to offer a wider variety of products to their customer base, Garn-St. Germain created more opportunities for savings institutions to compete with commercial banks.

112. See Financial Institutions Deregulation and Monetary Control § 10-231 (CCH 1980).
113. See id.
114. See id.
115. See id.
8. The Tax Reform Act of 1986

The Tax Reform Act (TRA)\(^{117}\) made dramatic changes for every corporate income taxpayer. The impact is no less for the banking industry . . . . Specific areas of the '86 Act aimed at the banking industry include net operating losses, bad debt expenses, disallowances of interest expense for excluded municipal obligations, favorable reorganization rules, and special depositor casualty loss rules. [There are, however,] questions in many areas that still must be answered through regulations, rulings and perhaps even court cases.\(^{118}\)

The advantages of the TRA for commercial banks and certain savings institutions which acquire a financially troubled savings institution were twofold. First, these acquisitions were exempt from certain reorganization and carryover rules.\(^{119}\) Second, “net operating losses” could be calculated differently, allowing a commercial bank to carry certain losses under net operating losses forward for fifteen years, and an acquiring savings institution to carry net operating losses forward eight years.\(^{120}\) Tax-free reorganizations were given certain concessions on bad debts, taxable income, interest expenses, contributions by FSLIC to an acquiring institution excluded from that institution’s gross income, and, under certain circumstances, the continuity-of-interest test was simplified for mergers or reorganizations.\(^{121}\)

119. See id. at 94-95.
120. See id.
121. See id. at 91. "For tax years beginning before Dec. 31, 1986, commercial banks could compute a bad debt deduction using either the direct charge-off method, allowing a deduction for those debts that had become partially or entirely worthless during the current tax year, or a reserve method, allowing a deduction for specific additions to a reserve for a tax year." Id. Under the TRA, the percentage method would not be available for tax years beginning after 1987. For tax years beginning after Dec. 31, 1986, large commercial banks could no longer use the reserve method to compute their bad debt deduction. (Under TRA, a bank is considered a "large commercial bank if the average adjusted bases of all its assets exceed $500 million or if it is a member of a parent/subsidiary controlled group with adjusted bases of all assets in excess of $500 million.) Small commercial banks (those with gross assets of $500 million or less), could continue to use the reserve method." Id.

"There is a suspension of the recapture for any tax year during which the bank is considered financially troubled. A bank is financially troubled if the average of its non-performing loans exceed 75% of its average equity capital for the year." Id. The cut-off method as articulated by the TRA is—once the reserve has a zero balance any recoveries will be taxable income and bad debts will be deductions. The election, therefore, means that no income from recoveries or deduction for bad debts is applicable until the reserve is reduced to zero. Savings institutions, (which include mutual savings banks, cooperative banks, and domestic building and loan associations), may use the specific charge-off method or the reserve method. See id.

[Therefore] as a result of the TRA, the applicable percentage of taxable income was reduced from 40% to 8%. [In addition,] this method would be available only if 60% of the savings institution’s assets are qualified under [the old requirements of the Internal Revenue Code of 1954]. For tax years beginning after Dec. 31, 1986,
The TRA altered the treatment of losses by depositors at troubled financial institutions. According to the new rules,

a reasonably estimated loss on a qualified deposit with a qualified financial institution incurred by a qualified individual due to the bankruptcy or

the interest expense to carry tax-exempt interest income securities acquired after Aug. 7, 1986 will no longer be deductible. This rule will apply to all commercial banks [and savings institutions]. The disallowance covers all amounts that could be allocated as tax-exempt interest expense.

Id. The average adjusted basis was to be the assets' tax basis plus the adjustments contained in new TRA § 1016. The old Internal Revenue Code of 1954, pertaining to a 20% tax-exempt interest disallowance, will continue to apply to securities acquired after Dec. 31, 1982, and before Aug. 8, 1986. The 20% rule reduces the deductible interest expense allocated to indebtedness incurred to purchase or carry tax-exempt obligations by 20%. See id.

The old Net Operating Loss (NOL) carryforward and carryback rule allowed financial institutions to carry their NOL's back for 10 years and forward for five years. This rule is repealed for all NOL's incurred in tax years beginning after calendar year 1986. The new rule allows NOL's of financial institutions to be carried back for three years and forward for 15 years. However, there are some special additional rules. [For commercial banks], the portion of the NOL for any tax year beginning after Dec. 31, 1986 and before Jan. 1, 1994 that is attributable to the deduction allowed for bad debts will have a special carryback period of 10 years and a carryforward period of five years. Other losses of a commercial bank will be carried back three years and forward 15 years under the new rules.

Id. As for savings institutions, for tax years 1982 through 1985 the savings institution may have a carryback period of 10 years and a carryforward loss period of eight years. See id.

Special rules [enacted under the Economic Recovery Tax Act of 1981—ERTA, 26 U.S.C. § 1221] exempted the acquisition of financially troubled savings institutions from the general reorganization and carryover rules. These rules provided that the continuity-of-interest test was satisfied for tax-free reorganizations, and the NOL's could be carried forward, if the depositors of the financially troubled thrift become the depositors of the surviving thrift. These rules specifically exempted from gross income payments of cash or property contributed by the Federal Savings and Loan Insurance Corporation. In addition, [these] payments from FSLIC did not reduce the basis in the assets of the target financially troubled thrift. If certain conditions were met, ERTA provided that the continuity-of-interest test was satisfied for mergers involving savings institutions. The first condition was that the institution must be a thrift, which included mutual banks, savings and loans and cooperative banks. The next condition was that the savings institution must have been certified insolvent by a state authority, the FSLIC or the Federal Home Loan Bank Board. An insolvent [savings institution] was one that could not meet its obligations currently nor for the immediate future. The final condition was that substantially all the depositors and other holders of liabilities of the transferor institution had to become the obligors of the transferee institution. When all of these conditions were met there was no need for any stock or security distributions by the acquiring institution to the acquired institution in order for the transaction to qualify as a tax-free reorganization.

Id. “ERTA had created a special provision for financially troubled thrifts: they did not have to reduce basis in their assets for money or other property payments from the FSLIC under its financial assistance program. In addition, the amounts received from the FSLIC were not considered income to the thrift.” Id. These special reorganization rules for financial institutions, enacted under ERTA were all repealed by the TRA for reorganizations occurring after Dec. 31, 1988, in tax years ending after that date. See id.
The insolvency of the institution will be deductible as a casualty loss at the election of the individual. [A] qualified individual includes all persons except a person who owns at least 1% in value of the outstanding stock of the qualified financial institution, an officer of the qualified financial institution, or any person who is related to another person or entity that owns at least 1% of the outstanding stock or is an officer of the qualified financial institution. A qualified financial institution includes commercial banks, thrifts, savings and loans, cooperatives, and any other similar institution chartered and supervised under federal or state law, [including] credit unions whose deposits or accounts are insured under federal or state law.\textsuperscript{122}

Other areas of the TRA had limited or no impact on most financial institutions: the compliance and administrative sections, the foreign tax credit calculations and limitations, and some of the personal income tax changes, which will probably affect the way banking services are used or delivered.\textsuperscript{23}


"Prior to the passage of the [Financial Institution Reform, Recovery and Enforcement Act of 1989 (FIRREA)],\textsuperscript{124} federal savings and loan institutions . . . were chartered and insured by a single entity, the Federal Home Loan Bank Board (FHLBB).\textsuperscript{125} FIRREA, signed into law on August 1, 1989, abolished the FHLBB and FSLIC, splitting the responsibility for chartering and insuring savings institutions between two agencies.\textsuperscript{126} The FDIC assumed control of the bankrupt savings and loan insurance fund and transferred it to the newly created Savings Association Insurance Fund (SAIF), which was kept separate and distinct from the Bank Insurance Fund (BIF), the fund that insures bank deposits.\textsuperscript{127} "A newly created arm of the Treasury Department, the Office of Thrift Supervision (OTS), assumed all of FSLIC’s regulatory responsibilities, which include examining and regulating all savings and loans and chartering federal savings and loans."\textsuperscript{128} The OTS, however, did not take over the responsibilities of the FHLBB until sixty days after the enactment of FIRREA. National commercial banks are subject to regulation and examination by the Office of the Comptroller of the Currency, the Federal Reserve System, and the FDIC.

Section 5 of the Home Owners Loan Act of 1933\textsuperscript{129} authorized the FHLBB to “give primary consideration (when granting a charter) to the best

\begin{footnotes}
\item 122. Id. at 96.
\item 123. See id. at 97.
\item 125. MACEY & MILLER, supra note 31, at 93.
\item 126. See id.
\item 127. See id. FIRREA also created the Federal Housing Finance Board which has the power to supervise federal home loan banks. 12 U.S.C. § 1422 (1994 & Supp. 1996).
\item 128. Id.
\end{footnotes}
practices of thrift institutions in the United States." Now that FHLBB was no longer in business, the OTS was given that charge and, like its predecessor the FHLBB, OTS was to grant a thrift charter only:

1) to persons of good character and responsibility;\textsuperscript{130}

2) if in the judgement of the director (of OTS) a \textit{necessity} exists for such an institution in the community to be served;\textsuperscript{131}

3) if there is a reasonable probability of its usefulness and success;\textsuperscript{132} and

4) if the association can be established without undue injury to properly conducted existing local thrift and home financing institutions.\textsuperscript{133}

Therefore, despite the differences in statutory language between the chartering standards used by the Comptroller of the Currency for granting charters to banks and the chartering standards used by the OTS for granting charters to thrifts, the substantive standards became very much the same.\textsuperscript{134} By two different routes, the two agencies emerge at about the same point. Both face "a short list of general standards in the relevant statutes for charter approvals, which are either too narrow or too unspecified to serve as much of a guide for restraint upon the exercise of [agency] discretion."\textsuperscript{135}

FIRREA proved inadequate to address industry concerns. One purpose for the creation of FIRREA was to further control and moderate the entrance of large banking organizations into markets already well served, certainly a purpose the climate of national banking cried out for. Instead, this particular purpose was frustrated because these newly created statutory directions given to the OTS to restrict new charters were no different from the previous rule of FHLBB or the prior requirements directed to the Comptroller of the Currency for banks to follow. The passage of FIRREA was in part a direct result of the perceived degree of fraud and insider abuse in the S&L industry and because the OTS and the FDIC became more aggressive in their attempt to recoup lost funds.\textsuperscript{136}

In the post FIRREA era, the number of San Diego savings institutions continued to decline. California banking organizations who had been willing during the 1980s to acquire the financially-troubled prodigious S&Ls were

\textsuperscript{130} See generally Eric G. Zajac, \textit{FIRREA and Federal Common Law: The Extent to Which they Preempt State Law Regarding the Duties and Standard of Liability Imposed Upon Financial Institution Directors}, 37 Vill. L. Rev. 1461, 1466 (1992) (maintaining that this was of vital importance to the FDIC, OTS, and FHLBB, because even though federal common law and state law articulated different standards for when directors/officers should be held accountable, both federal and state law held a bank director to owe fiduciary duties to depositors).

\textsuperscript{131} See \textit{Macey \& Miller}, supra note 31, at 93.

\textsuperscript{132} See id.

\textsuperscript{133} See id.

\textsuperscript{134} See id.


\textsuperscript{136} See id.
no longer seeking these vulnerable institutions, having been temporarily gratified by their already secured conquests. The large failing or closed savings institutions were no longer saleable, their liabilities contributing to the collapse of FSLIC. The Resolution Trust Corporation, the OTS, and the FDIC encountered increasing difficulty in locating buyers for these beleaguered savings institutions without offering major deal enticements. Additionally, the degenerating California real estate market complicated the regulator's ability to appropriate these losses. FIRREA was not helpful to regulators because it essentially continued the status quo. It gave no new tools to the regulatory agencies to deal with the S&L crisis.

10. Federal Reserve Act

The three commercial bank leaders in San Diego are subject to certain restrictions under the Federal Reserve Act. Transactions and extensions of credit between these banks and their subsidiaries are regulated by the Federal Reserve Board of Governors. There is a specific formula limiting the payment of dividends by these banks to their parent organizations or holding companies, which must be approved by the Comptroller of the Currency. The Federal Reserve Act requirements affect many areas of banking, allowing the Board to regulate electronic fund transactions, check collection, equal credit opportunity and truth-in-lending rules, and the provision and availability of funds.

Under Federal Reserve Board regulations, [certain banks] are . . . required to maintain reserves against their transaction accounts (primarily checking and NOW accounts). Because these reserves must be maintained in cash or in non-interest bearing accounts, the effect of the reserve requirements is to increase an institution's cost of funds. . . . [Financial institutions may designate and exempt [certain reservable liabilities] from these reserve requirements. These amounts and percentages are subject to adjustment by the FRB. . . . [D]epository institutions maintaining reservable accounts may borrow from the Federal Reserve Bank discount window, but the [FRB's] regulations require a savings bank to exhaust other reasonable alternative sources before borrowing from the Federal Reserve Bank.138

11. The Federal Deposit Insurance Corporation Improvement Act of 1991

The Federal Deposit Insurance Corporation Improvement Act, (FDICIA), was enacted December 19, 1991, but certain portions of its requirements did not become effective until December 1992. The Act provided for increased funding for the FDIC Bank Insurance Fund by assessment fees

on insured deposits.\textsuperscript{140} It also required establishment of a risk-based assessment system by January 1, 1994.\textsuperscript{141} FDICIA contained provisions for new reporting requirements, real estate lending and capital adequacy requirements, and expanded regulation for depository institutions and their parent holding companies.\textsuperscript{142}

In addition, FDICIA established a system of corrective action for any insured institution that falls below specified minimum capital levels.\textsuperscript{143} The highlight of this legislation was “the establishment of a five tier capital requirement system;” the tiers were “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized,” and “critically undercapitalized.”\textsuperscript{144} The Act did not define the capital levels for each of these terms, deferring instead to the federal financial regulatory agencies to specify these levels by September 1992, and requiring these agencies to take “prompt corrective action” on the banks which failed to meet minimum capital requirements.\textsuperscript{145} Capital distributions, such as the paying of dividends, were prohibited if the organization already was, or doing so would make, the organization undercapitalized.\textsuperscript{146} The ramifications for undercapitalization included limitations on the depository institution’s activities and an obligation to return the institution’s capital to regulatory standards.\textsuperscript{147}

When FDICIA was first passed, the implications on commercial and savings institutions were not clear. The financial regulatory agencies had yet to act and quantitative measures of capital had not yet been defined. By 1996, the large commercial banks had generally deciphered how the Act would affect them.

For example, Wells Fargo determined that “[f]ailure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the [bank’s] financial statements.”\textsuperscript{148} The quantitative measures established by the regulators to ensure capital adequacy required that Wells Fargo maintain minimum ratios of capital to risk-weighted assets. There were two categories of capital under the guidelines.

Tier 1 capital includes common stockholders’ equity, qualifying preferred stock and trust preferred securities, less goodwill and certain other deductions (including the unrealized net gains and losses, after applicable taxes, on available-for-sale investment securities carried at fair value). Tier 2 capital includes preferred stock not qualifying as Tier 1 capital, mandatory

\begin{itemize}
\item \textsuperscript{140} See id.
\item \textsuperscript{141} See id.
\item \textsuperscript{142} See id. See also WELLS FARGO & CO., 1996 ANNUAL REPORT 69 (1997).
\item \textsuperscript{144} Id. §§ 1817, 1825.
\item \textsuperscript{145} Id.
\item \textsuperscript{146} See id.
\item \textsuperscript{147} See id.
\item \textsuperscript{148} WELLS FARGO & CO., 1996 ANNUAL REPORT 69 (1997).
\end{itemize}
convertible debt, subordinated debt, certain unsecured senior debt issued by the Parent [or the holding company] and the allowance for loan losses, subject to limitations by the guidelines. Tier 2 capital is limited to the amount of Tier 1 capital (i.e., at least half of the total capital must be in the form of Tier 1 capital). Under the guidelines, capital was compared to the relative risk related to the balance sheet.\textsuperscript{149}

As a by-product of FDICIA, most financial institutions in their annual reports, and as part of most regulatory required reports, render an opinion of their capital regulatory position. For example, in its 1996 Annual Report, Wells Fargo offered the opinion that the bank had met all capital regulatory requirements to which it was subject, and reported the most recent Office of the Comptroller of the Currency notification categorized the bank as “well capitalized.”\textsuperscript{150}

The effect of FDICIA was calculated to be the same on all San Diego commercial banks, including market leaders Union Bank, BankAmerica, Wells Fargo, and the other depository institutions.

\textbf{12. The Riegle-Neal Interstate Banking \& Branching Efficiency Act of 1994}

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994\textsuperscript{151} amended the Federal Deposit Insurance Act. It was federal legislation that allowed for interstate banking transactions, bank branching, mergers, and acquisitions. Pursuant to Riegle-Neal, federal banking agencies would begin to approve the above described activities between insured banks with different home states without regard to state law so that the resulting institution could be operated as one bank with interstate branches. There were branching requirements, filing, notice and concentration stipulations, community reinvestment and operational considerations, and capital and management adequacy requirements. The federality of Riegle-Neal did not usurp the state tax implications of a branch or bank located in a state that was merged or acquired by an out-of-state bank.

On June 1, 1997, Riegle-Neal permitted national banks to branch nationwide, even in states which had not yet enacted legislation allowing that right to their own state-chartered banks.\textsuperscript{152} The Office of the Comptroller of the Currency ruled automated teller machines (ATM), remote service units (RSU), and even automated loan machines (ALM) do not constitute bank “branches” under the National Bank Act.\textsuperscript{153} In effect, that decision creates opportunities for banks to expand ATM, ALM, and RSU network systems without consideration of state-imposed restrictions on bank branching. What was left undecided, however, was whether and what other effects these op-

\textsuperscript{149} Id.
\textsuperscript{150} Id.
\textsuperscript{152} See id. § 1831(u).
\textsuperscript{153} See Comptroller of the Currency, Interpretive Letter No. 772 (Mar. 6, 1997).
opportunities would have on amalgamation activity.

The Riegle-Neal Act became effective on September 29, 1995, one year after being signed into law by President Clinton. Among other things, the bill allows for the continuation of certain state powers, amendment of state law to conform to this new federal law, and permits state governments to opt-in or opt-out of allowing interstate branching before June 1, 1997. States could begin waiving the state concentration requirements, but never the national requirements. So under Riegle-Neal, bank holding companies which were adequately capitalized and managed were permitted to engage in interstate acquisitions and mergers of banks and S&Ls, usurping the state restrictions. Banking organizations hailed Riegle-Neal as their own symbolic victory in the increasingly competitive financial business world.

13. California State Regulations—Riegle-Neal Act

During 1987, “a number of states enacted or amended interstate banking laws.” As of May 23, 1997, 47 states plus the District of Columbia and Puerto Rico had acted on interstate branching under the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994.” California permits statewide branching. Under legislation effective October 2, 1995, California permits a financial institution to opt-in to interstate branching through the acquisition of a California bank or consolidation of previously owned California banks. The legislation “prohibits de novo interstate branching as well as the acquisition of individual branches and places a five year minimum-age requirement on interstate bank acquisitions.” “This law also allows affiliate banks to act as agents for each other and eliminates discriminatory provisions in the bank holding company statute.” Riegle-Neal allowed banks to fully enter the securities market, in turn increasing competition in the investment industry and leading to improved services and lower costs for consumers.

Even prior to Riegle Neal, “beginning July 1, 1987, California permitted

155. See id.
157. Interstate Banking—All But Few States Beat Trigger Date On Nationwide Branching, 16 NO. 11 BANKING POL'Y REP. 11 (June 2, 1997) [hereinafter Interstate Banking].
159. See Interstate Banking, supra note 157, at 12; see also Geographic Expansion—All But Few States Enact Laws Approving Interstate Branching, 16 NO. 5 BANKING POL'Y REP. 5 (Mar. 3, 1997).
160. Interstate Banking, supra note 157, at 12.
161. Id.
162. See Tart, supra note 12, at 949.
out-of-state banking organizations to acquire in-state banking organizations, provided an out-of-state banking organization's home state granted similar privileges to banking organizations in California. The targeted reciprocal regions included eleven other Western states, Alaska, Arizona, Colorado, Hawaii, Idaho, New Mexico, Nevada, Oregon, Texas, Utah, and Washington. As a result, progressive California banking organizations originally concentrated their activities and merger deals in these states. "The California regional reciprocity limitation was dropped and the state opted into full reciprocal interstate banking nationally on January 1, 1991. The law also was extended to thrift institutions, except there was no provision allowing out-of-state banking organizations to acquire California thrifts."

It was pursuant to Riegle-Neal that Wells Fargo was able to complete its merger with First Interstate of California in 1996. First Interstate held bank subsidiaries in six states, Idaho, Nevada, New Mexico, Oregon, Utah, and Washington, and each of these states had opted-in early under the interstate branching aspects of Riegle-Neal. "Even though state-chartered banks in states that took no action before the trigger date [only Kansas, Missouri, and Wisconsin] lack authority to engage in interstate branching, national banks may now branch in and out of those states." As a consequence, Wells Fargo, BankAmerica, Union Bank, and even the smaller San Diego banking organizations and savings institutions began to acquire and invest in businesses, expand their retail base, and make loans without regard to state lines.

"The greatest movement toward expansion of banking powers has occurred at the state level.... State laws began to change, however, when banks began to realize that competition was inevitable and interstate expansion could be beneficial if organized through regional banking centers." States were permitted to control how an out-of-state bank could operate its branches as long as there was no discrimination against these out-of-state banks or bank holding companies. These state-imposed conditions were inapplicable after May 31, 1997. "Most states [began to use] a combination of two main types of restrictions when enacting interstate banking statutes: (1) 'regional restrictions' requiring the expanding bank to be located in a specific geographic region, and (2) 'reciprocity restrictions' requiring that the state of the acquiring bank allow acquisitions within that state by banks in the state allowing expansion."

Without the federal regulation of banking organizations, protecting the

164. Id.
166. Interstate Banking, supra note 157, at 11.
167. Tart, supra note 12, at 936.
168. See id. at 939-42.
169. See id.
170. Id. at 936.
national economic health would be left in the hands of bankers. From the stock market crash of 1930 to the savings and loan scandal and the deregulation of the 1980s, this country has consistently proven the need for federal bank regulation. Riegle-Neal, FDCIA, FIRREA, DIDMC, BHCA, and BMA are but just a few examples. Despite the growth and innovation demonstrated by San Diego banking organizations in the 1980s, a greater number of the local bank and savings institution failures and economic hardships would have resulted from decreased regulatory freedoms.

Yet regulation which "has come from both the federal and state governments constrained the expansion of [banking organizations] and contributed to the widespread failure of individual institutions." In the final analysis, the regulatory system may have impeded the growth of the American banking industry, but it has also protected the commitment of financial institutions to the economic well being of their local communities and their depositors.

B. Capital Adequacy Regulations for Banks and Savings Institutions: The Effect on San Diego Institutions

The ultimate question for the San Diego financial institutions that were trying to meet FDIC and FSLIC capital requirements became how capable were they of servicing their debt while maintaining capital above the minimum required levels?

1. Capital Adequacy Requirements for Banks

Capital regulation involves a comparison of a banking organization's assets and liabilities. A financial institution's capital represents the excess of its assets over its liabilities, or its cushion available to cover potential losses. There are different types of capital, some more tangible than others, and different types of assets, some riskier than others. The purpose of capital regulation is to insure that financial institutions do not fail for not being able to cover their losses.

Federal regulations require that depository institutions maintain specific levels of minimum capital. The National Bank Act specifies that national banks start with an initial capital, the amount of which varies depending on the location of the banking organization. However, the Comptroller of the Currency, which has supervisory authority over national banks, requires a higher level of startup capital than is mandated under the statute.

All capital stock must be paid in before the banking organization is authorized to do business. The law also generally requires that no insured

171. Reforming Financial Systems, supra note 4, at 85.
depository institution may make a capital distribution if such institution would be undercapitalized after making the distribution. The FDICIA system of corrective action requires “undercapitalized” institutions to submit capital restoration plans to their supervisory agencies. The capital restoration plan must specify steps that the institution will take to restore capital adequacy, set goals for capital restoration, and provide further information regarding the activities that the institution will engage in while restoring capital to a satisfactory level. If the capital restoration plan is not approved or complied with, then the “undercapitalized institution is restricted in its asset growth and must receive prior regulatory approval for business expansion plans.”

More stringent limitations are applied to institutions deemed “significantly undercapitalized.” Federal regulators are required to implement corrective action to get capital levels elevated to specified minimums. Such corrective action can include restricting transactions with affiliates or restricting the interest rates that the institution pays on deposits. Action can also include “improving management, prohibiting deposits from correspondent banks, or any other action” that the agency determines will ultimately raise capital levels.

Finally, institutions classified as “critically undercapitalized” are subject to the most onerous regulatory constraints. Unless the FDIC approves, these institutions may not enter into any material transaction other than in the usual course of business. Moreover, a critically undercapitalized institution cannot extend credit for any highly leveraged transaction or make any material change in accounting methods. Early closure is also specifically required for critically undercapitalized institutions if they do not improve their capital adequacy levels within ninety days from becoming designated as critically undercapitalized.

Aside from FDICIA’s classification scheme of undercapitalized institutions and attendant system of corrective action, there are currently two separate capital adequacy rules imposed on federal depository institutions. The first capital adequacy rule is a leverage ratio. A leverage ratio compares the “gross ratio of capital to assets without any adjustment for risk.” The federal regulatory agencies require depository institutions with high ratings to

175. See id. § 1830(o).
176. See id.; see also id. § 1464(t)(6)(A)(ii).
178. 12 U.S.C. § 1464(s)(4)(A)-(B) (1994 & Supp. 1996) (requiring the Director of the OTS to take actions with respect to undercapitalized savings institutions and the Comptroller of the Currency to do the same with respect to undercapitalized national banks).
179. MACEY & MILLER, supra note 31, at 296.
181. See id.
182. See id.
183. MACEY & MILLER, supra note 31, at 302.
have “core” capital, such as common shareholder’s equity, equal to 3% of adjusted total assets for the highest rated institutions. Depository institutions with lower ratings are required to maintain leverage ratios around 6%. For example, a low-rated banking organization with $100 million in assets should expect to maintain “core” capital equaling close to $6 million.

The second capital adequacy rule involves risk-adjusted capital ratios. Unlike leverage ratios that require banks to keep a minimum amount of capital per dollar of assets, risk-adjusted capital ratios analyze the type of asset held by a depository institution. The entire asset-side of a banking organization’s ledger is adjusted to reflect the risks associated with the assets.

In short, the risk-adjusted capital ratio involves a three-step process. The first step is to sort each depository institution’s assets into one of four different risk categories. Each category then carries the following weight: (1) zero percent for assets deemed essentially risk-free, such as loans backed by the full faith and credit of the U.S. government; (2) twenty percent for slightly more risky assets, like loans conditionally guaranteed by the U.S. government; (3) fifty percent for still more risky assets, such as first mortgage residential loans; and (4) one hundred percent for all other assets, which include private sector loans and bank-owned real estate.

The total assets in each category are then multiplied by the applicable risk-weight, and the products are summed. To illustrate, if a banking organization had $100 million in loans guaranteed by the U.S. government, then there would be no adjustment to the $100 million. However, if the federal banking organization had $100 million in first mortgage residential loans, then their assets would be adjusted by $50 million. This adjustment reflects multiplying the $100 million in assets by the 50% risk weight.

In addition, the guidelines also account for off-balance sheet items. These items, such as letters of credit or identity of the borrower, “are multiplied by a credit conversion factor to determine the ‘credit equivalent value.’” The FDICIA legislation also requires regulatory banking agencies to revise their risk-based capital standards to take adequate account of interest-rate risk. These risk-adjusted capital adequacy ratios did not originally account for interest-rate risk.

Once total assets are adjusted to reflect their associated risks, the second step is to calculate the depository institution’s capital. Capital is divided into two categories: (1) “core” capital, known as Tier 1 capital; and (2) “supplementary” capital, identified as Tier 2 capital. As stated earlier, “core” capital includes common shareholder’s equity. Tier 1 capital also includes

185. See id.
186. See MACEY & MILLER, supra note 31, at 303.
187. Id.
188. See Federal Deposit Insurance Corporation Insurance Act § 305(b)(1)(A)(I).
189. See MACEY & MILLER, supra note 31, at 303.
190. See id.
"noncumulative perpetual preferred stock and minority interests in equity accounts of subsidiaries." But, Tier 1 capital does not include the goodwill of the institution.192

"Supplementary" capital, on the other hand, represents debt or equity instruments that are deemed to be more ephemeral or to have less certain value than the components of core capital.193 This type of capital includes allowances for loan and lease losses, subordinated debt, and preferred stock not included in Tier 1.194 The total capital is then determined by adding "supplementary" and "core" capital.195 However, there is a limitation that the total of Tier 2 capital cannot exceed the total amount of Tier 1 capital.196

Finally, the third step in the risk-adjusted capital ratio is to determine whether the depository institution's total capital exceeds the mandatory minimum percentage of total risk-adjusted assets.197 Under this comparison, a ratio of 8% total capital to total risk-adjusted assets, effective December 12, 1992, is required.198 In other words, the minimum total capital that a depository institution must maintain is established by multiplying its total risk-adjusted assets by 8%. The guidelines in effect also require a separate "core" capital to a risk-adjusted assets ratio of 4%.199 To illustrate, if an institution had total risk-adjusted assets of $200 million, then its minimum total capital would be $16 million and its minimum Tier 1 capital would be $8 million.

The regulatory banking agencies originally believed that they would disregard leverage ratio requirements once risk-adjusted capital ratios became effective. However, these agencies decided to retain the leverage ratios. Thus, leverage ratios currently represent an additional level of capital adequacy that every federal depository institution must maintain.

2. Capital Adequacy Requirements for Savings Institutions

Having examined capital adequacy requirements for national banks, it is apparent that savings institutions’ capital rules are quite differently enforced and applied by bank examiners. For federal capital adequacy requirements, savings institutions include savings and loans, thrifts, and savings banks.200 Again, the savings and loan industry is supervised and regulated by the OTS, a subsidiary office within the Department of Treasury. Congress, under the Financial Institutions Reform, Recovery and Enforcement Act of 1989, im-

191. Id. at 303-04.
192. See id.
194. See id.
195. See id.
196. See id.
197. See id. §§ 461-483; see also id. § 1464(s)-(t).
198. See id.
199. See id.
200. See id. § 1464(t)(1)(A).
posed rigorous capital adequacy standards on the savings industry. 201

FIRREA subjects federally insured savings institutions to three capital adequacy requirements. 202 First, savings institutions, must have a 1.5% tangible capital to total assets ratio. 203 Tangible capital consists primarily of cash, stocks, and property. 204 Thus, tangible capital represents items that can be seized by a federal regulatory agency, in the event of a savings institution failure, before federal insurance funds are tapped. For this reason, tangible capital does not include "goodwill," which is the value of an institution's customer base and reputation.

The second capital adequacy requirement imposed on federal savings institutions is a 3% leverage ratio. 205 This means that federal savings institutions must have a gross ratio of capital equal to 3% of assets without any adjustment for risks. For example, if a savings institution has $100 million in assets, then it must have at least $3 million in capital to satisfy federal regulations. Even though 3% represents the statutory minimum, most savings institutions are required to maintain a 5% leverage ratio. 206

Finally, there is a risk-based capital requirement applicable to federal savings institutions, comparable to the risk-adjusted ratio imposed on national banks; but FIRREA additionally provides that the standards must not be less stringent than the capital standards applicable to national banks. 207 In other words, savings institutions must maintain at least 8% total capital to risk-adjusted assets. This provision has created controversy because it places the fate of many savings institutions in the hands of the Comptroller of the Currency, an agency that regulates national banks. The Comptroller can, in effect, regulate savings institutions by adopting stringent capital requirements for national banks.

While FIRREA has been heralded for imposing rigorous capital standards on savings institutions, the statute has not been promulgated without criticism. One criticism is that FIRREA emphasizes book value net worth. 208 Federal savings institutions are permitted to list their assets and liabilities at the price they paid for them, and not at their current fair market value. 209 The overall effect is that assets are listed by a federal savings institution to satisfy capital adequacy requirements with assets not representing their current fair market value. Thus, the book value of assets listed by a federal savings institution could be vastly inflated when compared to their actual value.

201. See id. § 1464(t)(2)(C).
202. See id. § 1464(t)(2).
203. See id.
204. See id. § 1464(t).
205. See id. § 1464(t)(2).
206. See id. § 1464(t).
207. See id. § 1464(t)(1)(C).
209. See id.
A second criticism is that the statute does not require higher deposit insurance premiums for higher risk investments.\textsuperscript{210} For example, savings institutions can maintain the same level of insurance premiums for loans guaranteed by the U.S. government, recognized as having no risk weight, as they can for private sector loans having a risk weight of 100%. But, in 1994, Congress, in an attempt to minimize the high-risk investments of savings institutions, passed legislation requiring savings institutions to dispose of junk bonds, the high-risk, high-yield debt securities, from their portfolios. In spite of these criticisms, it can be reasonably said that FIRREA has been instrumental in stemming the tide of savings institution failure so prevalent in the late 1980s.

The scope of FIRREA is not, however, limited to federal savings institutions. In California, the Department of Financial Institutions imposes analogous capital adequacy requirements on state-chartered savings institutions. At present, there are six California state-chartered savings institutions. California state savings institutions are required to make double regulatory fee payments, one to the Office of Thrift Supervision and one to the California Department of Financial Institutions.\textsuperscript{211} As a result of converting to federal charters to avoid the extra regulatory fees, very few state-chartered institutions remain.\textsuperscript{212}

Currently, “the powers and investment authorities of state-chartered institutions are virtually identical to those of federally chartered savings institutions.”\textsuperscript{213} In fact, state-chartered savings institutions must adhere to federal regulations promulgated by the Office of Thrift Supervision before they can operate in California.\textsuperscript{214} These institutions must also satisfy California statutory net worth requirements.\textsuperscript{215} The net worth, or capital, may not be less than 3% of an institution’s total assets.\textsuperscript{216} In defining total assets, the California Commissioner of Financial Institutions has great latitude. The Commissioner may issue regulations to exclude from the total assets any item deemed appropriate.\textsuperscript{217}

If the capital of a California savings institution falls below the statutory 3%, then the Commissioner may require the institution to increase its net worth so as to bring the amount to a level determined adequate under California law.\textsuperscript{218} Any state savings institution may be required to do any one or

\begin{itemize}
  \item [210.] See id.
  \item [211.] See CAL. FIN. CODE § 270 (West 1989 & Supp. 1998).
  \item [213.] Great American Shifts to Federal Savings Bank, ORANGE COUNTY REGISTER, July 3, 1990, at C03.
  \item [214.] See CAL. FIN. CODE § 5606(c) (West 1989 & Supp. 1998).
  \item [215.] See id. § 660.
  \item [216.] See id. § 6475(b).
  \item [217.] See id. § 660(b).
  \item [218.] See id. § 6475(b).
\end{itemize}
more of the following: (1) increase liquid assets; (2) stop accepting savings accounts of all classes or categories; (3) cease all lending; (4) stop the purchase of loans; (5) stop or limit promotional expenditures; (6) convene a meeting of its board of directors to accomplish these objectives; and (7) take any other steps that the Commissioner deems necessary to protect the interest of the institution and the public. 219

In sum, regulatory guidelines for state savings institutions are promulgated primarily by the federal government. But a state regulatory agency is empowered with authority to take corrective action if the state savings institution falls below required state statutory capital requirements. The federal government regulatory guidelines are imposed on California savings institutions, but state law ultimately provides the remedies that are applicable to these savings institutions if they do fall below the requisite minimum capital adequacy requirements.

National banks, federal savings institutions, and California savings institutions are subject to objective capital adequacy requirements. However, the State of California does not impose an objective criteria on its state-chartered banks. Like state savings institutions, state banks are also regulated by the Department of Financial Institutions. The Department, created in 1997, combines the previously separate licensing and regulation of banks, savings institutions, credit unions, and investment loan companies.

This Department generally requires that starting a bank in California requires about $5 million in start-up capital. 220 In addition the new bank needs experienced management who will be acceptable to state regulators. At the beginning of 1992, there were 262 California state-chartered banks with approximately $110 billion in assets. 221 In May 1994, the California State Banking Department reported that “California’s state-chartered banks increased their assets from $103.28 billion to $110.58 billion from December 31, 1990 to December 31, 1993. During the same time period, the average capital-to-asset ratio increased from 7.41% to 8.31%; and increased capital is always a positive sign for California’s consumers.” 222

Differing from the capital ratios imposed on national banks, California banking regulations focus on a bank’s “core” capital. State law examines several factors in determining whether a bank’s “core” capital, principally its shareholder equity, is adequate. Ultimately, the California Commissioner of Financial Institutions must consider the following factors regarding a bank’s “core” capital: (1) nature and volume of the bank’s business; (2) amount, nature, quality, and liquidity of its assets; (3) amount and nature of its liabilities; (4) amount and nature of its fixed charges; (5) history of, and prospects for, the bank to earn and retain income; (6) quality of the bank’s op-

219. See id. §§ 660, 8450(b). See also 9 CAL. JUR. 3d Banks § 305 (1993).
221. See Fitch, supra note 212, at 12.
222. CAL. STATE BANKING DEPT., 84TH ANNUAL REPORT (May 31, 1994).
eration; (7) quality of the bank's management; (8) nature and quality of its ownership; and (9) any other relevant factors. 223

These factors are subjective when compared to the capital adequacy standards imposed on federal depository institutions. Due to this subjectivity, state-chartered banks do not have a uniform minimum capital adequacy requirement. To illustrate, a rural bank will likely have lower capital adequacy requirements than a bank located in a big city. The volume of the rural bank's business is less than the city bank's volume. Correspondingly, the nature of the rural bank's assets and liabilities are usually smaller. These facts may compel the state regulatory agency to impose lower capital standards on the bank located in the rural community.

Another important consideration in determining the capital adequacy is the state bank's management. Management that is comprised of individuals knowledgeable about operating a bank will be regarded more highly by the regulatory agency than inexperienced management or management that has a disreputable history of operating banks. Thus, the Department of Financial Institutions will more likely impose lower capital adequacy standards on a bank that is under management acceptable to state regulators.

Although these factors examining "core" capital can be described as subjective, state banking law requires banks to make periodic reports and submit their records to examination by the Commissioner's office. 224 These reports must be submitted from all California state banks no less than once every two years. 225 The reports itemize the assets and liabilities of a state bank, thus enabling California regulatory agencies to determine whether "core" capital requirements are satisfied.

In addition, these reports create a certain objectivity in California banking regulation. If the Department of Financial Institutions finds that one of its state-chartered banks is undercapitalized, then it can take corrective measures comparable to those imposed on state savings institutions to prevent the bank from failing. Strengthening the veracity of these reports is the fact that if a California deputy commissioner of the Department of Financial Institutions learns of a bank's insolvency but fails to report it, then he or she is guilty of a felony. 226

Basically, California savings institutions follow objective capital adequacy requirements applicable to federal savings institutions. These state savings institutions adhere to the three capital standards imposed by the Office of Thrift Supervision on all federal savings institutions. National banking institutions, like federal and state savings institutions, are also subjected to objective capital adequacy requirements.

California banks, on the other hand, have their capital adequacy re-

---

224. See id. § 1900.
225. See id. § 1900.3.
226. See id. § 1910.
requirements determined by subjective factors promulgated by the California Department of Financial Institutions. These factors do not reflect the complexity of the capital adequacy ratios imposed on national banks. However, the recent stability of federal and state banking organizations and savings institutions underscore the point that different types of regulatory schemes have been effective in minimizing failures of these financial institutions.

C. What Happened to Financial Institutions When Minimum Capital Regulations Were Not Met

It was the inability or failure to maintain adequate capital which led to the dissolution of a significant number of banking organizations. The push for higher capital ratios resulted in chaos for smaller savings institutions. The only source of capital for small savings institutions is retained earnings, so their growth is slowed while they push to rise to new minimums. This in turn caused these small savings institutions to lose market share to the larger commercial banking organizations who had the ability to borrow to meet new capital levels without slowing their own growth. Savings institutions, which tend to lend to consumers and small businesses with less credit worthiness, are required to charge off potential losses against earnings... further reducing the savings institutions capital. Small banks and S&Ls must either replace these charge-offs with new capital or shrink the level of credit they can provide.227

The failure of many banks and savings institutions connected with non-bank-related business ventures resulted in a legislative response of specific limits designed to safeguard bank stability in the economy.228 Yet, from 1985 to 1996, there were sixteen financial institution failures in San Diego County. (See Appendix B.)

IV. WHY FINANCIAL INSTITUTION MANAGERS & DIRECTORS CHOSE AMALGAMATION TO PROMOTE GROWTH

Management practices are really what control the financial industry. "[B]anking can't blame public policy, can't really blame the economy for its problems. It can blame itself for failing to exercise proper private sector disciplines. We should have learned to expect public policies not to be very smart—in most times—very politically driven, very expediently driven. In the management side of this equation, we had competition in laxity. Unfortunately the dumbest and weakest competitors in the marketplace set the basic standards of pricing and credit terms."229 Management decisions were at

228. See Tart, supra note 12, at 916.
the heart of the banking failures of the past. However, management practices are also the force driving the current merger and acquisition environment. “In the final analysis, the socialization of the risks underlying credit (the democratization and liberalization of credit to everyone, cheaper credit, more liberal credit) ultimately falls back on the people.”230 The negative effects of amalgamation also “falls back” on the bank customer.

In many cases, amalgamation is a practical management decision for financial institutions. But a combination of many factors was responsible for this choice as an expansion technique. Changes in federal and state regulation, eliminating geographic boundaries, new product development, expanding banking powers, and national, regional and local economic developments, are all factors in a financial institution’s plans to diversify their business and compete more directly with nonbank financial concerns.

Regulatory constraints, even after deregulation and Riegle-Neal, made amalgamation a difficult task. “[T]he history of U.S. banking in the twentieth century can be partly read as an attempt to escape regulation.”231 It became obvious, however, to financial institution executives that negotiating the maze of banking regulation to win approval of a merger or acquisition was well worth the corporate profits that their increased market share would provide. Thus, “banks used legal loopholes to acquire other banks, changed the law if they could, and when they failed, created surrogate forms—bank holding companies and chain banks . . . . [L]arger financial institutions were built [in this way], particularly in California.”232

Financial institutions most often cite the following reasons for making a decision to merge or acquire another banking organization.

A. Decision Motivators

1. Increased Ability to Compete

Amalgamation increases competition and profitability. Increased competition enhances financial institution opportunities in the marketplace and increases the efficiency and soundness of all banking institutions.233 Financial institutions also believe amalgamation will increase financial strength.

2. Increase Number of Depositors

While antitrust matters are a concern, the banking industry clearly sees interstate banking as a tool to expedite growth. In order to expand into interstate banking and branching, commercial banks and savings institutions were

230. Id.
231. Reforming Financial Systems, supra note 4, at 86.
232. Id.
233. See Tart, supra note 12, at 947.
initially willing to sacrifice some profitability in exchange for large increases in accounts, potential deposits, and customer base. Even before Riegle-Neal, in 1992 well capitalized federally chartered savings institutions were allowed nationwide branching by the Office of Thrift Supervision. Such interstate branching alone tremendously increased an institution’s customer base.

3. Efficiency

Greater efficiency would result from amalgamation. “Under the new branching provisions [of Riegle-Neal], [bank holding companies could] merge all affiliated subsidiary banks into branches, eliminating the need for separate boards of directors, computer systems, record keeping, other banking technologies, and the extra costs associated with owning separate businesses. These cost savings could be used to replenish bank capital, thus increasing the ability to absorb losses,” and meet regulatory capital requirements.235

4. Tax Implications

There were certain non-direct benefits of these cost savings to taxpayers. The Tax Reform Act of 1986 offered certain incentives for calculating net operating losses which occur in connection with the acquisition of another institution. Possibilities like reducing the strain on the FDIC insurance fund, reducing regulatory burdens on banks, and possible deposit insurance reform were not outweighed by the potential pitfalls such as compliance with stricter consumer protection laws, notice and filing requirements, and additional costs imposed on newly-formed interstate branches by requiring state or federal Community Reinvestment Act (CRA) compliance.236

5. Market Position

Branch banking would enable national and state-chartered banks to expand their deposit bases and loan service areas and increase potential for growth. Arguably, the greater diversity would lead to greater security if a certain banking area or region were to become financially unstable.237

6. Product Development

The Glass-Steagall Act238 restrictions were relaxed in the 1990s, allow-

235. Tart, supra note 12, at 944.
236. See id.
237. See id. at 945.
ing banking organizations the ability to offer certain security and investment products directly to their customers. An increased customer base provided more opportunities and need for a greater array of banking products.

7. Regulatory Flexibility.

Savings institutions were able to diversify without conforming to the stricter rules placed on commercial banks by the regulatory agencies. Also, antitrust concerns have been somewhat relaxed by the financial regulatory agencies.

V. THE GROWTH OF FINANCIAL INSTITUTIONS THROUGH AMALGAMATION

Between 1925 and 1945 the number of savings institutions fell from a peak of roughly 12,500 to about 6,700. In the same period the number of banks fell from about 30,000 to 14,000. The decline reflected the large number of institutions that failed after the [stock market] crash and during the depression and the mergers that ensued as the turmoil tapered off, the economy stabilized, and banks and thrifts became more conservative in their business strategies. Then the good times reigned. For the next twenty years, beginning with a veteran-driven home-buying boom at the end of World War II, the [savings institution] industry prospered.239

By the 1980s, financial institutions again began to die. "In 1985, 120 federally insured banks failed, the highest number since 1933 . . . . This contrasts sharply with an average of four failures per year in the sixties, eight per year in the seventies, and ten failures in 1981 . . . . [A]bout 1,100 of the 14,500 commercial banks are considered ‘problem banks,’ that is, banks having a significant chance of failure."240 This situation created plenty of opportunities for large banking organizations to merge or acquire the troubled institutions.

In the mid-1980s several major San Diego savings institutions converted from federal savings and loans to state-chartered savings banks, Great American and Home Federal among them. In 1987 there were thirteen state-chartered savings banks doing business in San Diego.241 Coast Savings and Loan Association and Great Western Bank led this group with twenty-four and nineteen branches respectively.242 California regulatory law offered tools to state chartered savings institutions that many other states did not. There was greater flexibility in licensing, examination, supervision, and enforcement. Put simply, California regulatory law created an environment that both encouraged expansion and permitted savings institutions to move rapidly

239. DAY, supra note 34, at 50.
242. See id.
into what, for them, were new areas of business. In this climate, several of the savings institution subsidiaries became significant profit-centers and were better positioned as state corporations than as federally regulated service corporations. The California regulatory structure originally administered by the California Financial Code gave way to a Department of Savings and Loan headed by a commissioner with "general supervision over all associations, savings and loan holding companies, service corporations, and other persons." But by the fall of 1994, the trend was away from state-chartering of savings institutions and the California Department of S&Ls was downsized by then Governor Pete Wilson to only four employees (an Interim Commissioner, an examiner, a staff analyst, and a part-time assistant) who regulated state-wide only fourteen state-chartered savings institutions. The Office of Savings and Loan no longer performed audits of state-chartered savings institutions and was restricted to simply a review and analysis actually performed by the federal Office of Thrift Supervision.

Between the mid-1980s and early 1990s, the opportunities for amalgamation existed, the state and federal regulatory scheme promoted such activity, profits from amalgamation were apparent, financial products were expanding, and the larger institutions were well leveraged; it was obvious: tremendous growth was achievable through amalgamation and it was the right time to begin.

VI. SAN DIEGO FINANCIAL INSTITUTIONS IN 1985

San Diego was one of the first places amalgamation was successful. Banking organizations doing business there were catalysts for merger and acquisition activity in this country and for how banking is now organized. The most recent mergers to affect the San Diego community are the 1998 BankAmerica/NationsBank and Wells Fargo/Norwest mergers. They are, for the moment, the last Southern California examples of the continued amalgamation of banking organizations.

Largely because the primary growth product for savings institutions, and to a lesser degree for banks, are home mortgages and housing development loans, the impact of amalgamation in San Diego logically began with the housing market. Housing development grew at a phenomenal pace into the San Diego suburbs during the mid-1980s. "One in every eight home sales in the United States in 1985 occurred in California." San Diego residents spend approximately 33.3% of their income on housing, compared to 28% spent by consumers nationally. Consumers began locating their accounts and banking more in the areas in which they lived. San Diego bank-

ing organizations, which were in a growth mode, quickly built retail branches in these newly populated suburban areas. Strategic planners at San Diego financial institutions saw these banking customers as their future. Management of these institutions also sought retail branch networks and individual branches either through mergers with, or acquisitions of, banks that already had retail systems well positioned in these areas. This was one rapid response to service those quintessential affluent financial institution customers. There were fierce battles from 1985 through the 1990s among San Diego banks and savings institutions for growth-oriented, home-owning, dual income depositors, who regularly made large durable goods purchases. Clearly, these were the depositors to court if a bank or S&L was to survive and ultimately prosper in the San Diego economy.

Southern California banking has always been distinct from banking in the rest of the country. From the pioneering use of ATMs in Southern California, to widespread amalgamation beginning in the early 1980s, San Diego has been on the forefront of the financial industry’s progression.

While banking organizations throughout the country were in a continuous state of turmoil, the 1980s were a time of tremendous growth and prosperity for the financial institutions doing business in the San Diego market. In 1985 in San Diego, BankAmerica was the Commander of commercial banking; Home Federal and Great American were the savings institution Generals. Locally based savings institutions particularly experienced high profitability. Great American posted a lending volume of $3,874,244 for 1986, and by December 31, 1986, were calling themselves “the [seventh] largest publicly-held FSLIC-insured savings institution in the United States, based upon assets as of December 31, 1986.”

San Diego Trust had assets of $1,341,190, a total of $1,194,305 in deposits, 1,400 employees, and forty-eight branches as of December 31, 1986. Home Federal reported a healthy $103,358 net income, a total income of $1.2 million, and 3,640 employees, while Wells Fargo reported $44,577 million in assets and loans of $36,771 million at year-end 1986. Wells Fargo still had not entered the San Diego market in a big way. BankAmerica reported $91,606 million in assets, liabilities of $87,825 million, and $75,998 million in deposits at December 31, 1986.

Those sixteen banking organizations, major players in the San Diego market in 1987, had already been reduced in number substantially by 1992. “[P]ublic policy [had] shifted to a clear and substantial favoritism toward big

247. GREAT AMERICAN OFFERING CIRCULAR, supra note 38, at 17.
252. See supra note 9 for a listing of the sixteen organizations.
banks—a favoritism that [was] especially lethal at a time when small banks [were] under severe competitive pressures from geographic and pricing de-
regulation.\textsuperscript{253} “The latent effect of deregulation was to move the basis of
competition onto those parts of the playing field (economies of scale, price, tech-
technological product development) in which the larger institutions excelled,
and away from those aspects (personal service, convenience, community
emphases, etc.) in which smaller institutions had traditionally been stronger.
Many small banks were willing to pay a price for the opportunity to compete
more effectively on their own terms. But they made the mistake of assuming
deregulation meant just that, less regulation, not more. They also assumed
that the regulations remaining in force would be administered even hand-
edly. But deregulation, as it evolved, meant disproportionately higher costs
of doing business for small banks.”\textsuperscript{254}

In 1985, the primary business of savings institutions in San Diego was
lending for improvements on, or the purchase and construction of, residential
and commercial properties secured by first and second liens. Typically these
loans, secured by single family dwellings, multifamily residences, construc-
tion loans, commercial and light industrial properties, and loans made for the
acquisition and development of unimproved property, were the focus of
savings institution business in the 1980s. This was due largely to regulatory
constraints imposed on savings institutions prior to 1980 that limited long-
term permanent, fixed interest rate loans on residential properties.\textsuperscript{255}

Garn-St. Germain and the deregulation acts broadened the scope of S&L
lending activities, consumer products, and commercial banking powers.\textsuperscript{256}
Both deregulation and Garn-St. Germain had the effect of dramatically in-
creasing competition by narrowing the distinctions between savings institu-
tions and banks. Under deregulation, the cost of funds and interest rate sen-
sitivity was intensified and ultimately increased, leading to the termination
of differentials in interest rates on deposits between savings institutions and
commercial banks by January 1, 1984.\textsuperscript{257} However, most savings institutions
recognized, even as they diversified their lending activities, that profits
would be impaired as a direct result of deregulation of deposit liabilities be-
cause of the number in their portfolios of long term loans with either fixed
interest rates or adjustable rates. These loans had narrow features that would
hinder the savings institutions from adjusting yield on its loans to offset the
increase in the market interest rates on their sources of funds.

After these Acts were passed, savings institutions began to diversify by
expanding the types of products and accounts they could offer. S&Ls pro-
moted a new array of consumer and commercial loans, from home equity,
mobile home, home improvement and education loans, to auto, recreational

\begin{itemize}
\item \textsuperscript{253} Rau, \textit{supra} note 227.
\item \textsuperscript{254} \textit{Id}.
\item \textsuperscript{256} \textit{See}, \textit{e.g.}, \textit{Id.} § 1464.
\end{itemize}
vehicle, boat, credit card loans, and secured and unsecured commercial busi-
ness loans. Deregulation also prompted savings institutions to venture into
the making and purchasing of more adjustable rate mortgages and to in-
tcrease their fee income by servicing loans for other financial institutions.
Savings institutions were highly skilled in this area since servicing had been
such an intimate aspect of their loan maintenance activities. Amid this finan-
cial climate and the beginnings of amalgamation activity, savings institutions
found their loan servicing skills highly marketable and lucrative.

From 1985 to 1989, a lower national interest rate environment caused
savings institutions to experience a marked increase in the local origination
of both fixed-rate and adjustable-rate mortgages. Heightened consumer pref-
erences and competitive pressure during this period created a climate in
which savings institutions were able to continue and to increase their utiliza-
tion of devices such as due-on-sale clauses in fixed-rate conventional mort-
gages, origination fees, late fees and prepayment clauses, and even introduce
other fee generating novices such as loan modification and change of prop-
erty ownership fees. Income realized from these fees proved to be significant
for the San Diego-based savings institutions.

Most California and San Diego savings institutions attempted to re-price
and restructure their match of assets to liabilities using their knowledge of
historical market product performance. They increased their participation in
reverse repurchase and interest rate swap agreements, limited their invest-
ments in mortgage-backed securities, and used cap agreements to try and
manage interest rate risk. Some were more successful than others. Great
American managed to regulate their match of assets to liabilities to around
2% between December 31, 1984, and December 31, 1986.258 Some measured
their results differently. Home Federal's results were a 7.3% increase of total
assets from December 31, 1986, to June 30, 1987, and a net income of
$26,600 for the same period.259 San Diego Trust had a return on assets of
.83%, a slight decrease from 1989 results.260 On June 30, 1987, Imperial
Savings was one of the largest thrifts with $10 billion in assets and $5.5 bil-
lion in deposits.261 The commercial banks were somewhat more successful.
According to the San Diego Business Journal, Wells Fargo was still not a
major player in the San Diego market in 1986.262 BankAmerica held the
strongest position of the commercial market leaders in 1987 with assets of
$93 billion and deposits of $76 billion.263

259. See Top Area Savings and Loan Associations, SAN DIEGO BUS. J. BOOK OF LISTS 79
   (Dec. 1987).
261. See Top Area Savings and Loan Associations, SAN DIEGO BUS. J. BOOK OF LISTS 79
   (Dec. 1987).
262. See Top 25 Area Banking Companies, SAN DIEGO BUS. J. BOOK OF LISTS 29 (Dec.
   1987).
Effective December 15, 1987, the Financial Accounting Standards Board (FASB) issued new accounting rules which altered the accounting procedures for non-refundable fees and costs associated with both originating and acquiring loans through mergers or acquisitions. The new rules required loan origination fees to be deferred and attributed to income over the life of the loans, instead of being recognized at the time of origination. These FASB regulations focused on the timing of reporting fees and expenses. There was no effect upon fee income generated from borrowers, or loan origination and purchase loan costs, however certain loan origination costs were now required to be capitalized and amortized just as loan fees were.

During this time, FSLIC insurance regulations limited the maximum amount secured by real estate that a savings institution could lend to any one borrower and that borrower's related business/personal entities, to the lesser of that institution's regulatory net worth or 10% of the institution's separate net withdrawable accounts.264 However, on August 15, 1986, the FHLBB, as operating authority of FSLIC, proposed amending the regulation limiting aggregate loans to one borrower by reducing the limitation to 25% of regulatory capital.265

"Government regulation sheltered [savings institutions] from competition [prior to deregulation], allowing the industry to be profitable and failures to be rare. As long as interest rates did not rise substantially, [savings institutions] faced little risk."266 "Federal deposit insurance was provided as a subsidy allowing savings institutions to raise large amounts of funds at less than market interest rates so that they could finance long-term, fixed rate, home mortgage loans."267 It was in this climate that several of San Diego's hundred-year-old S&Ls first prospered greatly and then, after deregulation, ultimately failed.

All of these factors indicated that financial institutions in the mid-1980s would have to design new ways to prosper. Because of a few national and local successes, increasingly the directors and executives of San Diego banking organizations began to look to amalgamation as a means to increase profits.

A. Successes and Impacts of Initial Merger and Acquisition Activities in San Diego

It was no aberration that amalgamation began with savings institutions in the San Diego area. In 1985, the three major San Diego born and bred S&Ls, Great American, Home Federal, and San Diego Trust, were well-capitalized, self-assertive, strategically-located in the national and California

265. See id. § 1828.
266. ORIGINS & CAUSES, supra note 42, at 1.
267. Id.
banking market, and keenly aware of the market opportunities deregulation had provided. They began at that time to take advantage of their strength in the market and expand by merging. The first banking organization to do so was Great American Bank. Perhaps coincidentally, Great American was home to both “Lawrence Taggart, California’s . . . Commissioner of Savings & Loans [in 1983], who worked for twelve years for [the bank, and] Gordon Luce, CEO and Chairman of the Board of Great American, [Ronald] Reagan’s confidant and thrift guru, [who was] later appointed by Reagan to be a delegate to the United Nations.”

1. Great American First Savings Bank

Great American completed the sale of its retail branch network to Wells Fargo and was closed by the OTS in August 1991. Headquartered in San Diego, the bank was originally organized in 1885, as a California mutual stock institution under the name San Diego Building and Loan Association. In 1936, the bank converted to a federally chartered mutual savings and loan association and changed its name to San Diego Federal Savings and Loan Association. To reflect its expanded market area, San Diego Federal changed its name to Great American Federal Savings and Loan Association in 1982. After the implementation of the provisions of the Garn-St. Germain Depository Institutions Act of 1982, Great American changed its designation from a savings and loan association to a savings bank, and assumed the name Great American Federal Savings Bank. Because California law was more favorable to savings institutions, in 1983 “Great American converted from a mutual [savings organization] to a stock form of ownership . . . .” In July 1984, “Great American became a California licensed savings bank, changing its name to Great American First Savings Bank, under which it operated until its demise.

Like most California savings institutions, Great American’s deposits were insured by the FSLIC, governed by the provisions of the California Savings Association Law, subject to the regulations of the California Savings and Loan Commissioner, and Great American was a member of the

268. DAY, supra note 34, at 131, 175.
270. See supra note 17 (describing the differences in types of savings institutions).
271. California law provided greater freedom of business to savings institutions. The capital ratios were lower, the political climate favored management decisions to merge and acquire other banking organizations, but there was a double regulatory fee (if the savings institution was state-chartered)—one fee paid to OTS and one fee paid to the California Department of Financial Institutions. See supra Part III.B.
273. See id.
Federal Home Loan Bank System.\textsuperscript{274} When it acquired Home Federal Savings and Loan Association of Tucson, Arizona, it became a savings and loan holding company and thus subject to the holding company regulations of the FSLIC.\textsuperscript{275} At year-end 1986, the bank believed itself to be the seventh largest FSLIC-insured savings institution in the United States\textsuperscript{276} and operated 190 branch offices,\textsuperscript{277} sixty-one of those branches in San Diego county.\textsuperscript{278} In 1986, Great American Bank had 600,000 customers and offered 100 products and services to them.\textsuperscript{279}

Again, as with most California savings institutions, Great American was primarily involved in the business of "attracting deposits from the general public and using [those] deposits, [along] with borrowings and [other] funds . . . , to make mortgage loans primarily secured by liens on residential and other real estate . . . [along with] consumer installment and business loans."\textsuperscript{280} The bank's income came from loan principal payments, interest on and fees in connection with real estate loans, interest and dividends on investment securities, increases in deposits, cash received as a result of the maturity of securities investments, securities sold under agreements to repurchase, mortgage-backed securities, advances from the Federal Home Loan Board, other borrowings, and the income received in connection with loan amortization, prepayments, loan sales, and participation in loans.\textsuperscript{281} Through its 180 retail offices in California and Arizona, and through its subsidiary corporations, the bank offered "insurance brokerage, mortgage origination, securities brokerage, advertising, marketing," a myriad of loan products and services, and real estate development.\textsuperscript{282}

Great American was the first savings institution in San Diego to use amalgamation as a tool to increase their market share. "In 1981 and 1982, Great American expanded its operations in California by merging with eight savings and loan associations."\textsuperscript{283} Prior to these mergers the bank reported total assets to be around $6 billion.\textsuperscript{284} By the conclusion of the first eight mergers, Great American's asset size increased to $8 billion.\textsuperscript{285} By 1986, the bank had completed 14 mergers within 16 years.\textsuperscript{286} However, the bank's last major merger was its downfall.

\textsuperscript{274} See Great American Offering Circular, supra note 38, at 17.
\textsuperscript{276} See Great American Offering Circular, supra note 38, at 17.
\textsuperscript{277} See id. at 18.
\textsuperscript{281} See Great American Offering Circular, supra note 38, at 18.
\textsuperscript{283} Id. at 2.
\textsuperscript{284} See id. at 41.
\textsuperscript{285} See id.
\textsuperscript{286} See id. at 2-4.
In March 1986, the bank acquired Home Savings and Loan Association of Tucson, Arizona. At first, the Home Federal merger appeared to successfully accomplish what amalgamation had done for Great American in the past. By June 30, 1987, Great American’s total assets were reported to be $13.7 billion, a 30.3% increase from December 31, 1986, with deposits of $9.2 billion and a net worth of $779,803 million.\(^{287}\) In connection with the Home Federal acquisition, Great American, through an agreement with FSLIC, also acquired Hacienda Federal Savings and Loan and First Federal Savings and Loan of Redding California, which were both insolvent institutions.\(^{288}\) On May 7, 1986, Great American acquired Los Angeles Federal Savings Bank and on March 9, 1987, the acquisition of First Security Savings and Loan Association of Grand Junction, Colorado, was completed.\(^{289}\) Also in 1987, the Bank completed its final merger with Capital Savings Bank, F.A., which had offices in the states of Washington and Montana.\(^{290}\) During 1986, the Bank had increased regulatory capital 49%, to $755 million, "positioning Great American with the seventh highest regulatory capital base in the industry."\(^{291}\)

At the end of 1986, Great American believed itself to be the seventh largest publicly held saving institution with $13.7 billion in assets.\(^{292}\) Then the real estate assets acquired in the Arizona market through the Home Federal merger bottomed out. Both the California and Arizona real estate markets took a huge downturn and Great American sold its entire California retail branch network in 1990 and 1991 to Wells Fargo Bank.\(^{293}\) Subsequently, the bank was taken over by the Office of Thrift Supervision in 1991.\(^{294}\)

Great American’s disappearance was Wells Fargo’s great emergence in the San Diego banking market. Wells Fargo’s acquisition of the Great American branch network brought the total of Wells Fargo branches to 612, 292 in Southern California alone at the end of 1991.\(^{295}\) At the end of the branch acquisition, Wells Fargo initially retained fifty-seven of the sixty-four San Diego Great American branches and twenty of its own twenty-six Wells Fargo San Diego branch offices. The number of San Diego branches fluctuated wildly throughout the following years with Wells Fargo closing some offices and acquiring more as it increased its own acquisition activities


\(^{289}\) See id. at 56.

\(^{290}\) See id.

\(^{291}\) Id. at 5.

\(^{292}\) See GREAT AMERICAN OFFERING CIRCULAR, supra note 38, at 17; see also Top 25 Area Banking Companies, SAN DIEGO BUS. J. BOOK OF LISTS, Dec. 1987, at 29.


\(^{294}\) See STATISTICS ON BANKING, supra note 3, at D-34.

in San Diego. Yet, Great American's 100+ years of citizenship in San Diego left indelible marks on the City, its real estate, the 4000+ San Diegans it had employed, countless community projects, and ultimately its depositors. Great American and savings institutions like it created certain expectations in the minds of depositors, as both bank customers and members of the San Diego community.

2. First National Bank

"National Bank of La Jolla and National Bank of Fairbanks Ranch merged with First National Bank on May 29, 1987." It was a total combination of the organizations yielding $382,075 million in assets: National Bank of La Jolla's $157,842 million in assets and First National's assets of $224,733 million. First National was established in 1981. By December 31, 1996, First National Bank had leveled out to $293 million in assets, and $263 million in deposits. The Bank currently has four local branches, 184 employees, and its primary activity is real estate lending.

3. Crocker National Bank

Crocker was the first bank to disappear from the San Diego market as a result of amalgamation. In 1986, Crocker National Bank became the first bank with a large presence in the San Diego market to be acquired by another financial institution, Wells Fargo Bank. Wells Fargo paid $1.1 billion in cash for Crocker. At the time of acquisition, Crocker had 319 branches in the state of California, approximately seven in San Diego county. Wells Fargo operated 517 branch offices, 187 in Southern California.

With this merger, Wells Fargo increased their market share of total deposits from approximately 1.5% of all deposits in the California financial market to 3.6%, making Wells Fargo, by their own assertion, the fifth largest domestic lender in the United States. Wells Fargo understood the benefits of amalgamation perhaps because the bank is the product of a merger itself. The Wells Fargo California banking business, originally founded in 1852, was separated in 1905 from the Pony Express stagecoach business and

297. See id. Total asset size of National Bank of Fairbanks Ranch at the time of merger unknown.
299. See id.
301. See id; see also Telephone Interview with Dan Conway, Vice President of Public Relations, Wells Fargo Bank (Apr. 27, 1998).
merged in 1960 with American Trust Company.304

It was during the Crocker merger in 1985 that Wells Fargo announced its intention to become a major regional banking company. Crocker made a major contribution to Wells Fargo's ability to target the San Diego market. In its 1986 Annual Report, Wells Fargo clearly stated that the bank's objectives were to increase competitiveness by expanding its retail presence in Southern California, more effectively marketing services, making inroads into specialized areas of wholesale banking in the California middle market, focusing on trade financing among Pacific Rim nations and the United States (especially trade moving through the West Coast), and moving into more commercial real estate development—particularly single-family housing projects,305 which traditionally had been the business of savings institutions.

Crocker had been the seventeenth largest bank in the United States at the time of acquisition by Wells Fargo.306 While the announcement of the deal was a shock to both the San Diego and the banking communities, Crocker's loss to the San Diego market did not cause continued anxiety because of the perceived advantages to be gained by Wells Fargo's entry.

4. Home Federal Savings & Loan

Home Federal was placed in RTC conservatorship and subsequently closed by the OTS in July 1992.307 In addition to amalgamation activity, selling and buying branches was also a popular way to consolidate market share and minimize competition among savings institutions and banks in the San Diego market. As it had done many times before in connection with Home Federal applications, on May 28, 1987, the FDIC approved the transfer of the Julian BankAmerica branch to Home Federal Savings and Loan. On the date of the transfer, Home Federal reported $8.2 billion in total deposits.308

As of June 30, 1987, Home Federal's total assets were reported to be $12.8 billion, a 7.3% increase in total assets from December 31, 1986; $9.1 billion total deposits and $11 billion in loans.309 With fifty-two branch offices in San Diego, a net worth of $854 million, and 4,223 employees, the savings institution was second in San Diego only to Great American.310

By early 1991, Home Federal appeared to be having difficulty servicing its debt while maintaining capital above the minimum required levels, lead-

307. See STATISTICS ON BANKING, supra note 3, at D-37.
308. See There is a Reason FDIC Decisions Are So Juicy, 6 No.17 BANKING EXPANSiON REP., Sept. 7, 1987, at 14.
310. See id.
ing to its closure. Ultimately, its own retail branch system was packaged and sold to various other banking organizations. Because of its philanthropic contributions, its competitive nature among other banking organizations, and its history in the city, the closure was a significant loss to the San Diego community and its depositors.

5. San Diego Trust and Savings Bank

Although First Interstate Bank's acquisition of San Diego Trust in 1994 was not one of the mergers that initially impacted amalgamation in San Diego, the impact of its leaving as the last large savings institution based in the city was of major significance to the community, its depositors, and the bank's employees. Of the dominant San Diego savings institutions, San Diego Trust was the only savings institution to be sought after and acquired while still financially healthy. At the time of the 1994 acquisition, San Diego Trust was also the last remaining of the three savings institutions311 that had, for decades, dominated the San Diego market.

Headquartered in San Diego, San Diego Trust was organized under the banking laws of the State of California, began to conduct business in 1889, and to provide trust services in 1929. San Diego Trust and Savings Bank was a subsidiary of San Diego Financial Corporation, a California corporation organized on July 7, 1969, to function as a holding company for the Bank.312 Unlike its San Diego competitors, San Diego Trust had the foresight to organize as a California corporation years before Great American and Home Federal. Executive management of San Diego Trust recognized early the advantages to being subject to the California Department of Savings rather than being a federal savings and loan.

In 1990, the bank regarded itself as the largest locally headquartered trust department with market value assets of $2.8 billion. The trust products offered included personal trusts, business trusts, which included retirement services, and investment real estate trusts. In addition, the bank provided trust security products like mutual funds, annuities, and investment advising through a full service securities brokerage affiliate, San Diego Trust Securities, Inc. and San Diego Financial Capital Management, Inc.313 The bank's basic array of services included business, money market and personal checking, an array of savings accounts, telephone banking, cash management services, certificates of deposit, commercial loans, personal business banking, lines of credit and business loans, home equity credit lines, equipment financing and leasing, receivable and inventory financing, auto loans, real estate construction loans, consumer loans, customer credit card services,

311. The largest last remaining savings institutions were San Diego Trust, Great American Bank, and Home Federal.
313. See id. at 6-7.
and merchant processing credit card services, the full gamut of traditional savings institutions products plus some.

As of 1990, the bank had a total of fifty-five offices and drive up locations in San Diego County and operated forty-eight automated teller machines throughout San Diego at leased sites not attached to branch offices. On December 31, 1986, San Diego Trust reported having 1400 employees.

In 1990, the bank reported a significant increase in earnings, income of nearly $13 million, a 3% growth from 1989 year-end, a total deposits increase of 10.4% over the previous year to $1,481 million, and increases to its loan portfolio of 9.7%, expressed in dollars as $72 million. Net interest income before loan losses increased 6% in 1990. Year-end total assets were reported as $1,629 million and deposits as $1,481 million. The bank was ranked as one of the fifty safest banks in the country, one of the ten safest banks in California, and the safest bank in San Diego County.

Collectively, these five initial mergers and bank transactions in the San Diego market incited aggressive amalgamation. However, "by 1992, a recession that negatively impacted real estate values was in full-swing, and a majority of the banks and thrifts in the southern part of the state, and some up north, were experiencing serious asset quality problems. The problems were so severe that between 1992 and 1995, 34 California commercial banks and 32 California savings and loans, with combined assets of about $24 billion, failed."

The California State Banking Department's 84th Annual Report noted that in 1993, seven state-chartered and nine federally-chartered banks failed in California; those banks included two state-regulated banks in the San Diego market, the Bank of San Diego, and First California Bank. "According to the report, the performance of California state-chartered banks improved in 1993 as compared to 1992; earnings were up 36% from the previous year and the aggregate return on assets and equity increased 0.44% and 5.3%, respectively; over 70% of state-chartered banks were profitable; state-chartered banks strengthened their capital positions and increased their loan loss reserves; cut back on construction lending, and total loans and leases were up a fraction in the last quarter of 1993, to $66.6 billion."

However, for the year of 1992, the State Banking Department found there was a net

314. See id. at 10-12.
315. See id. at 8, 32.
318. See id.
319. See id.
320. See id. at 3.
322. See STATE OF CALIFORNIA BANKING DEPT., 84th ANNUAL REPORT 6 (Dec. 31, 1993); see also Brenot & D'Angelo, supra note 154, at 112.
It was during this time that an amalgamation of the last large locally based San Diego savings institution occurred. San Diego Trust and Savings Bank agreed to First Interstate Bank’s merger offer in 1994.

VII. HOW AMALGAMATION AFFECTED THE SAN DIEGO COMMUNITY, FINANCIAL INSTITUTION CUSTOMERS, AND EMPLOYEES

[Around 1981,] the thrift industry was a mess. Technically it had failed. Of the country’s four thousand savings institutions, Bank Board officials estimated that only forty or fifty—at most maybe a hundred—were solvent. Even these struggled .... [M]ost of the big California [savings institutions], touted as the industry’s largest and healthiest, were hurting .... Nineteen eighty had been the first year in FSLIC history that its expenditures to handle problem cases exceeded its income from insurance premiums paid by the thrifts it insured .... California, Illinois and New York emerged as key problem states early on.

In San Diego, in spite of the industry’s condition, amalgamation was just beginning. The two large local S&Ls (Great American and Home Federal) had begun to utilize opportunities to acquire other healthy banking organizations. The major commercial banking organizations were actively researching other institutions of like size with product compatibility and similar business ideologies. The amalgamation that was to come in the late 1980s had begun to materialize. Its appearance had a major effect on San Diego.

A. Impact of Amalgamation on Financial Services Availability and Efficiency, Products, and Customer Service Culture

Prior to the San Diego Trust merger with First Interstate Bank of California, after which First Interstate was merged into Wells Fargo Bank, San Diego Trust was known as a local bank with excellent customer service. Customer service was a major focus of San Diego Trust business; the bank stressed to both employees and the public their commitment to providing prompt, personal, and efficient service. During 1990, a program called “Customer Comments, Opportunities to Improve” was implemented. The program specifically reacted to customer comments and suggestions and initiated internal operations changes in response to those comments. As part of that customer service emphasis, San Diego Trust offered “the largest full-service, card-accessed banking system” in the county of San Diego, which accommodated point-of-sale capabilities at Carl’s Jr. restaurants, ARCO gas

325. DAY, supra note 34, at 92.
stations, and local grocery stores. San Diego Trust claimed that its banking card "provided instant access to funds at virtually every type of ATM throughout the United States." San Diego Trust was the last major San Diego savings institution to continue to offer drive-up banking when the others had ceased to believe this service was cost effective.

Pioneer Mortgage Entities was a mortgage provider in the San Diego real estate market and a customer of San Diego Trust and Savings Bank. The company sold trust deeds to investors in exchange for the funds required to make the underlying loans, and made regular monthly payments to the investors as borrowers paid off the loans. This practice required a constant large cash flow. In the late 1980s during the Southern California real estate market downturn, Pioneer fell upon hard times. "Many of the company’s loans went into default, resulting in a shortage of incoming revenue. Pioneer continued to make advances to investors, but had to borrow money from several San Diego banks to stay in business."

Partially because of its customer service policies, the bank granted Pioneer "provisional credit" on all . . . deposits Pioneer made . . . to various commercial accounts it maintained at the bank. The San Diego Trust "provisional credit" service meant that "when Pioneer deposited checks into its account at [San Diego Trust], the bank posted a credit to Pioneer’s account and permitted Pioneer to withdraw the funds before the deposited checks cleared through the clearinghouse system." San Diego Trust regularly granted provisional credit to all of its customers in good standing, as did many other smaller banks in the San Diego area. In addition to allowing Pioneer this courtesy service (which Pioneer regularly utilized), the bank’s customer service included almost daily calls to Pioneer "to say that it needed a deposit to ‘cover’ the amount of checks presented for payment the previous day." Pioneer always brought in a covering deposit, and San Diego Trust always paid the checks. The problem was that the check Pioneer deposited to cover account “A” was drawn on another Pioneer account (ac-

327. See id.
328. Id.
330. See id.
331. See id.
332. Id. at 707-08.
333. Id. at 708.
334. The term “clearinghouse,” as used here, refers to a local organization that provides clearing, netting, or settlement services for all financial institutions which are members of the organization. Member banks exchange checks and other negotiable instruments for payments that were drawn on other member banks. The local organization usually performs this task through the regional Federal Reserve Bank. See generally id.
335. Id.
336. Id.
337. See id.
count "B") that did not have sufficient funds.\footnote{See id.}

There were, of course, formal allegations of check kiting made during Pioneer’s bankruptcy proceedings during 1997 in United States District Court, but the court ultimately found no fraudulent intent to exist on behalf of Pioneer or San Diego Trust.\footnote{See id. at 715-16.}

The type and extent of customer services San Diego Trust provided to Pioneer is not extended by the large financial institutions, and therefore hardly exists in the San Diego market. This kind of customer service culture is not a priority for over half of the sixteen financial institutions that remain in the banking business in San Diego. Without smaller financial institutions (commercial and otherwise) and large savings institutions, there is a noticeable void in the local market. The implications of the customer service culture of financial institutions on small businesses, minority- or women-owned businesses, or businesses which experience cash flow or financial problems because of market effects are compelling. Customer services are particularly important to the survival of the large number of small businesses and sole proprietorships that make significant contributions to the San Diego economy and employment rate.

San Diego Trust’s motto in 1990 had been "This City and this Bank Have Grown Up Together," to reflect their known customer service thinking.\footnote{See SAN DIEGO TRUST AND SAVINGS BANK, 1990 ANNUAL REPORT 6 (1991).} The motto was replaced with a new one which said “The Bank Where Money Matters, But People Count,” to reaffirm its commitment to the city of San Diego.\footnote{See id.} Like San Diego Trust, Great American also hailed customer service principles as central to their success. The bank regularly introduced new promotion campaigns directly targeting customer service goals. In 1986, Great American’s retail branch system, loan, finance, operations, and executive groups launched a new customer service campaign known as “C.A.R.E.: Customers Are the Reason We Exist.”\footnote{See GREAT AMERICAN FIRST SAVINGS BANK, 1986 ANNUAL REPORT 19 (1987).} The bank strongly believed it could hold its market share in an increasingly competitive marketplace by “affirming its principles of customer service” and offering “a diversity of products with a showing of respect, enthusiasm, and professionalism at each point of customer contact.”\footnote{Id.}

Even though merged banks insist they can nurture relations with small business borrowers while cutting costs, small business owners fear that mergers will bring conservative standards and a decline in personal service. Wells Fargo and other big banks say they “can maintain personal relations with business owners who demand it, while relying on automation to serve the rest.”\footnote{Michael Selz, Bank Mergers Reduce Loans to Small Firms, WALL ST. J., Mar. 10,} Three examples which suggest the opposite of that very idea

\begin{thebibliography}{9}
\bibitem{see} See id.
\bibitem{see1} See id. at 715-16.
\bibitem{see2} See SAN DIEGO TRUST AND SAVINGS BANK, 1990 ANNUAL REPORT 6 (1991).
\bibitem{see3} See id.
\bibitem{see4} See GREAT AMERICAN FIRST SAVINGS BANK, 1986 ANNUAL REPORT 19 (1987).
\bibitem{id} Id.
\bibitem{see5} Michael Selz, Bank Mergers Reduce Loans to Small Firms, WALL ST. J., Mar. 10,
\end{thebibliography}
follow:

In 1995, four years after Allied Irish Banks, PLC, acquired her company's bank, Ms. [Patricia] Cumor sought to double a $200,000 credit line that she had obtained [for her business] before the merger. In the past, [her business'] receivables secured the credit line .... [B]ut... the bank's new owner wanted additional collateral, including real estate her company owned as well as some of her personal assets.

... "My bank had changed and I was paying for it," [said] Ms. Cumor. When a bank representative told her, "My hands are tied," Ms. Cumor switched to an independent local bank.

....

During its acquisition of First Interstate Bancorp, Wells Fargo closed the San Diego branch that had served Linda Hanover's clothing and costume store. Ms. Hanover [said] she knew the branch's staff so well that the manager would call to warn her that a check might bounce. "There's no way that would happen" at the Wells Fargo branch that now handles her account. Ms. Hanover [said she was] switching to a savings bank that still operates a branch on her store's street. "There's a branch manager there who will talk to me," she [said.]

....

[There are still some occasional, but real attempts on the part of big banks to demonstrate their commitment to customer service. Prior to its merger with Washington Mutual, Great Western branch managers] hand-delivered nearly 1,400 pre-approved loan applications to business owners in California and Florida .... The promotion produced $22.5 million of loans to 752 borrowers. ....

[Last, in] October of 1996, Luis Hernandez's dental supplies exporting concern in Miami borrowed $50,000 from Great Western when a local branch manager called on him . .... While [Mr. Hernandez] has kept a commercial account with another bank that bought his old lender, he has never applied for a loan there. "I don't have a relationship with any people there," [said] Mr. Hernandez. "They never came to see me at all."

B. San Diego Amalgamation Antitrust Implications

Antitrust matters have increased in importance because of the unusually high number of financial institution mergers in San Diego, as opposed to merger activity in other industries and other geographic markets. The last ten years has seen a consolidation in the banking industry resulting in greatly reduced competition in San Diego. The large homegrown institutions are gone. 346 The out-of-town banks led by BankAmerica, Wells Fargo, and Un-
ion Bank, all got bigger by acquiring smaller banking organizations and now dominate the local market. Washington Mutual alone, from 1988 to 1997, acquired five banks which had done business independently in San Diego.

The banking regulatory agencies and the Justice Department both review the competitive effects of bank mergers. Often these agencies review the impact of a proposed merger from different perspectives, using different standards and reaching different results. Whatever their collective findings, the anti-competitive effects of a merger can always be remedied by a federal agency inspired divestiture plan. The Federal Reserve Board, FDIC, OTS, and the Office of the Comptroller of the Currency often focus on the CRA implications of a bank merger, variability in competition in the proposed merger market, the relevance of geographic and market products, economic measures of concentration, and mitigating factors of an increase in competition.

The bank regulatory agencies such as the Federal Reserve tend "to advocate bank mergers. In light of past savings and loan failures, the [FRB] favors banking consolidations in order to advance the safety and soundness of the banking industry. Conversely, the [Department of Justice (DOJ)], along with the Federal Trade Commission (FTC) tend to scrutinize mergers more closely. As a result at times, the FRB will approve a proposed merger and the acquirer will move forward under the impression that the application process is essentially complete. Then the DOJ will file suit based on antitrust implications of the merger, ... or delay the transaction based on potential anticompetitiveness in the post-merger environment." However, DOJ's ultimate focus is on how a particular transaction will affect competition. "[C]ompetitive problems are generally localized and can [usually] be resolved through targeted divestitures." The treatment of the Bank-America/Security Pacific merger is one example. "In [this] merger, the [DOJ] found that the divestiture of branches, vault and operational facilities, deposits and related earnings assets, such as commercial loans, in local markets in each of five states (Arizona, Nevada, California, Oregon, and Wash-

347. See id.
348. See id. The five acquired institutions were Pioneer Savings Bank, World Savings and Loan Association, Far West Federal Savings Bank, American Savings Bank, and Great Western Bank. See id.
350. See id.
ington) were sufficient to remedy likely competitive effects.\textsuperscript{353}

The Federal Reserve Board and the DOJ will also evaluate a bank merger’s impact using the Herfindahl-Hirschman Index.\textsuperscript{354}

No banks have litigated a merger case to conclusion in nearly a decade.\textsuperscript{355} A surprisingly minute number of bank merger cases are ever litigated at all, partially because the Bank Holding Company Act\textsuperscript{356} (BHCA) and Bank Merger Act\textsuperscript{357} (BMA) allow the Department of Justice to issue an automatic stay of a transaction when negotiating divestiture plans with merging bank organizations. Yet the DOJ often fails to give clear and uniform guidance on their enforcement policies as a regulator in this area.

The Federal Reserve Board will not approve any acquisition, merger, or consolidation that results in a monopoly, which would lessen competition or restrain trade, unless it finds that it would produce a public benefit that would outweigh these negative effects.\textsuperscript{358} Furthermore, the Board will take into account the resources of the company and the conveniences it would provide the community.\textsuperscript{359} In addition to the federal regulatory agencies, merging financial institutions must also take into consideration the views of state banking agencies that take an active role in amalgamation matters.

The California State Banking Department precludes the department superintendent from approving any application unless it is determined

that the public convenience and advantage will be promoted by the establishment of the proposed bank; conditions in the locality of the proposed bank... afford reasonable promise of successful operation; the bank is being formed for legitimate proposes; the capital is adequate; ... and the applicant has complied with all applicable laws.\textsuperscript{360}

One factor in each of the Federal Deposit Insurance Corporation’s decisions concerning acquisitions, mergers, branch sales, and purchases is always whether the transaction in question would have a significant impact or “adverse effect” on competition.

\textsuperscript{353} Id.

\textsuperscript{354} The HHI measures pre- and post-merger markets by adding the squares of each firm’s market share to arrive at an HHI value between zero and 10,000—where 10,000 is a pure monopoly. For banks, the total deposits are weighed in the market concentration measurement. For instance, if four merging firms (banks, for example) have a market share of 25% 25%, 35%, and 35% respectively, the HHI is calculated as \((25)^2 + (25)^2 + (35)^2 + (35)^2 = 3700\), resulting in a HHI total of 3700 points. \textit{See United States Department of Justice and the Federal Trade Commission, Horizontal Merger Guidelines} § 1.51 (Apr. 2, 1992; revised Apr. 8, 1997).


\textsuperscript{357} Id. § 1828.

\textsuperscript{358} \textit{See id.} § 1842(c)(1)-(2).

\textsuperscript{359} \textit{See id.}

\textsuperscript{360} Brenot, \textit{supra} note 39, at 102.
The FDIC considers the structure and planned implementation of the transaction in question, the number of commercial banking and savings organizations in the specific marketplace, how many offices each institution has in that marketplace, whether there are adequate banking alternatives, the particular organization's financial condition and managerial resources, the impact the consummated transaction would have on direct competition, earnings capacity, capital adequacy, Community Reinvestment Act issues, and possible adverse competitive effects. In addition, as the late [1980s] progressed, the FDIC increasingly reviewed real estate investment activities in connection with merger and acquisition activity.361

"The Federal Reserve Board uses similar criteria as the FDIC in its own merger, acquisition and even its bank holding company formation decision making processes."362 The Board’s overall objective however, is to insure that the proposed transaction not have a significant adverse effect on existing competition in the banking market under consideration.363

During 1988 the Federal Reserve Board made several merger and acquisition decisions that involved substantial competition problems. The transactions in question had the potential of eliminating a considerable amount of existing competition. However, in all cases the Board found off-setting circumstances such as a satisfactory number of competitors remaining in the market upon consummation of the proposed transaction, that a particular bank may not have been an aggressive competitor or active lender in the market, the concentration of bank resources in the market, the presence of thrift institutions in the banking market with the potential to become major competitors of commercial banks, and the convenience and need considerations of customers.364 Despite the Board’s standards, because of the offset analysis there have been very few denials of San Diego banking organizations’ merger applications on antitrust grounds.

The DOJ’s approach to competition was liberalized further by revisions made to its formal guidelines in 1997.365 "The overall effect of the revisions to the DOJ’s Guidelines is that the DOJ has abandoned its past rigid position in merger analysis by explicitly denouncing pure reliance on market structure as the primary indicator of anti-competitiveness. By moving toward a more flexible approach in the evaluation of proposed bank mergers, the DOJ has increasingly come to resemble the FRB as a facilitator of banking mergers. Although tension between the DOJ and the FRB still exists, the extent of their disagreements may narrow as the DOJ’s new Guidelines are applied in a more liberal fashion than permitted under prior Guidelines."366

363. See id.
364. See id.
365. See Kilian, supra note 351, at 858.
366. Id.
Arguably there are antitrust problems that now exist for certain banks in San Diego, but these problems already existed when the institutions made application to the Board to further their amalgamation activities.

From a bank perspective, California has become a "duopoly" with BankAmerica and Wells Fargo holding about one-third of the state's deposits and almost 60 percent of the commercial bank deposits. This domination was solidified when Wells Fargo's required divestitures in the First Interstate deal were allowed to go to a thrift. The next largest domestic bank has less than 1 percent of the deposits, and among the foreign banks, the Bank of Tokyo affiliate—Union Bank—is the leader with a 4.2 percent deposit share. No other foreign bank in California has more than a 1.1 percent share.  

Mergers are regulated by section 7 of the Clayton Act, which proscribes transactions that may substantially lessen competition or create a monopoly. Both the financial regulatory agencies and the courts use the authority of the Clayton Act and the Sherman Act in bank antitrust matters. The courts have some latitude to interpret the law, and recent decisions have varied from Consolidated Gold Fields v. Anglo American, in which a merger was enjoined because it marginally increased concentration in an oligopolistic industry, to United States v. Synfy Enterprises, in which a merger to near monopoly was considered legal due to the lack of entry barriers. All decisions are subject to review by the Supreme Court, but the Court did not review the merits of a merger case in the 1980s. Cases in this area focus on the likely effect of a merger, with emphasis on market shares, barriers to entry, efficiencies, and structural conditions affecting the outcome of federal court decisions.

Merger enforcement in the courts is generally based on United States v. Philadelphia National Bank, in which the Supreme Court ruled that high concentration established a rebuttable presumption of illegality. The level of evidence sufficient to rebut the presumption appears to have evolved over the years. The BMA and BHCA "convenience and needs" defense was largely a result of the Supreme Court's decision in Philadelphia National Bank. "The fact that the financial services industry is in the midst of a competitive and technological revolution makes it imperative that the DOJ and bank regulators take steps to analyze bank competition in a way that is not unduly dismissive of the speed with which the industry is changing." In the same case in which it analyzed a bank merger in "local" geographic markets,

367. Danielson, supra note 7, at 6-7.
368. 698 F. Supp. 487, aff'd, 1989-1 Trade Case (CCH) ¶ 68,500 (2d Cir. 1989).
372. Brian W. Smith & Mark W. Ryan, E-Banking Challenges Traditional Approaches To Antitrust Analysis, 16 No. 11 BANKING POL'Y REP. 1, *17 (June 2, 1997).
the Supreme Court also explained that the relevant product market was the "cluster of products and services" offered by commercial banks. But again, as time passed, different agencies developed different approaches, with the Federal Reserve Board and OCC favoring the cluster of services approach and the DOJ favoring "a disaggregated ‘business line-by-business line' approach to product market definition." The DOJ Horizontal Merger Guidelines were issued in 1992, governing mergers in all industries, including mergers involving banking organizations. However, the tension between the DOJ and regulatory banking agencies prevails.

Early Supreme Court decisions in cases such as U.S. v. [Von's Grocery Company] established almost a per se rule against mergers in concentrated industries, the [U.S. v. General Dynamics Corporation] decision highlighted the importance of competitive factors other than market share. The Court ruled that full consideration of a market's 'structure, history and probable future' was necessary to measure the competitive impact of a transaction, but the court decisions do not give any obvious way of weighing the various economic factors in the legal decision.

Obviously, this is also true of the financial regulatory agencies. The FDIC, OTS, the FRB, and the Comptroller of the Currency all consider economic factors a predominant factor in evaluating a banking organization's entry into a particular market, yet will part from a traditional application of antitrust law to approve an adverse bank combination if doing so addresses demonstrated public need. Financial regulatory agencies routinely consider these needs to be the provision of services otherwise unavailable from the existing financial institutions or eliminating an unhealthy, insolvent or non-responsive depository institution so as to strengthen the local banking market.

C. Impact of Amalgamation on the San Diego Economy

Staying competitive in the financial services industry continues to be a major concern nationally for both banks and savings institutions. Congress and the Federal Reserve Board have demonstrated some legislative intent for commercial banks and savings institutions to remain conscious and respectful of public needs while lobbying for amalgamation and product growth. From the beginning of San Diego amalgamation to date, the ability to offer competitive financial products and services in the banking and nonbanking realm drove commercial banks, and to a lesser degree the savings institu-

374. Smith & Ryan, supra note 372, at *17; see also Philadelphia National Bank, 374 U.S. at 356-57.
375. The 1992 DOJ Guidelines were revised and re-adopted by the DOJ in 1997.
378. Coate, supra note 370, at 3.
tions, to formulate annual strategic plans which focused on that goal. Such strategic planning, especially of the San Diego savings institutions, often led to a restructuring which included forming a corporate entity (a bank holding company) from which to operate both banking and nonbanking activities. Creating a holding company allowed savings institutions to diversify the products and services they were permitted to offer their depositors.

The Bank Holding Company Act of 1956\textsuperscript{79} was a Congressional response restricting bank holding companies from engaging in some nonbanking activities. Under the Glass-Steagall Act and the Bank Holding Company Act of 1956, the Federal Reserve Board must grant approval for a bank holding company to engage in activities "closely related to banking or managing or controlling banks."\textsuperscript{380} The Board grants this approval by examining two aspects of the activity. First, the Board determines whether the non-banking activity is "proper incident to banking or managing or controlling banks."\textsuperscript{381} Then, a second determination is made as to whether the activity is a "benefit to the public, as anticipated by the Act."\textsuperscript{382} Federal courts and the Board have determined that the public benefits test weighs the advantages of the proposed nonbanking activity against the possible adverse effects on the public by examining 1) whether banks generally "conduct the proposed activity;" 2) whether banks "provide services that are operationally or functionally so similar to the proposed activity as to equip them particularly well to provide the proposed services;" or 3) whether banks generally provide services "that are so integrally related to the proposed service as to require their provision in a specialized form."\textsuperscript{383}

The Board shall consider whether its performance as an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse affects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices.\textsuperscript{384}

Public benefit, therefore, remains central to the expansion of banking activities. The logical query then becomes whether the expansion of banking activities, one of the core reasons for the concentration of amalgamation in Southern California, has been beneficial to the public, i.e., the San Diego community.

\begin{footnotes}
\item[380.] Id. § 1843(c)(8); see also Part III.A.1.a.
\item[381.] Id.
\item[382.] Id.
\end{footnotes}
1. Has the Local Economy Benefited From Amalgamation?

In its 84th Annual Report, the California State Banking Department found that

[the California economy appeared to move in a positive direction in 1993; the state's unemployment rate fell to 8.8% from 10% earlier in the year, while the national average dropped to 6.3% from 7% during the same time period. . . . Other economic indicators began to show improvement; for example, retail sales in key urban areas of the state increased by 6%-8%. In 1993, sales of single family homes increased by 3.2% over 1992 figures.]

On December 31, 1997, the California unemployment rate stood at 4.3% and was projected to decrease to 4.0% by the end of 1998.

Central to San Diego's economy are the biomedical, military, aerospace, defense, electronics manufacturing, retirement communities, and tourism industries. Except for the addition of international trade, from 1985 to 1998 the economy has not changed. The city's economy is well-diversified and experiencing constant growth. The military payroll has a tremendous impact on San Diego's economy. Financial and business services have increasingly become a force in the past twelve years. Conservative estimates are that the county's economy will grow at a rate of 4% per year. In 1987, San Diego County had a $42 billion dollar economy, a figure larger than the economies of several states. Factoring in ten years of growth, the San Diego Chamber of Commerce estimates gross regional product alone will be over $88.7 billion by year-end 1998, outperforming both the state and the nation. What continues to fuel population growth, gross regional product growth, and housing construction is San Diego's strategic geographic location. Being positioned between Los Angeles and Mexico creates two huge markets in which San Diego can expand its economic success. "San Diego's international border crossings continue to be the busiest in the world, with 52.5 million crossings recorded in 1996 . . . . The San Diego International Lindbergh Field Airport reported 6.9 million passenger arrivals in 1996, a

385. STATE OF CALIFORNIA BANKING DEPT., 84TH ANNUAL REPORT 6 (Dec. 31, 1993).
386. Brent & D’Angelo, supra note 154, at 112.
387. See GREATER SAN DIEGO CHAMBER OF COMMERCE-ECONOMIC RESEARCH BUREAU, SELECTED SAN DIEGO COUNTY ECONOMIC INDICATORS (1998) [hereinafter SELECTED ECONOMIC INDICATORS].
389. See id.
390. See id.
391. See id.
392. See id.
393. See FUTURE SCAN, supra note 246, at 27.
394. See SELECTED ECONOMIC INDICATORS, supra note 387.
A high cost of living and the changes in the job market have adversely affected a significant portion of the local population. The average household income in San Diego at the end of 1997 was estimated to be $72,100, and is projected to be $75,000 by the end of 1998. Although the regional economy is strong, a significant segment of the population is being adversely affected by the high cost of living and the changing job market. This segment is growing, is becoming poorer, and is requiring more assistance from our community’s health and human care services.

Movements to stem population growth through residential development moratoriums may negatively impact the economy by reducing the amount of affordable housing and incurring losses in the construction industry. These growth initiatives, particularly a factor in the north and east county areas of San Diego, may negatively affect home lending activities for banks and S&Ls. Ultimately, however, population growth and in-migration will continue to create plenty of new opportunities for financial institutions because of San Diego’s favorable climate, proximity to Los Angeles and Mexico, and its quality of life. Even during the national recession in 1990, San Diego avoided the full impact of any economic slowdown because of its diversity, rapidly growing population, significant defense spending, and strong tourist industry.

The amalgamation of San Diego’s banking organizations has had relatively little negative impact on the local economy. Despite the demise of the three largest San Diego based savings institutions in the early 1990s, the San Diego economy continues to thrive. The market shares these savings institutions left was quickly absorbed by the big banks: BankAmerica, Wells Fargo, and Union Bank. Changes in employment, diminished competition, community support by banks, a lessening in the credit available to small businesses, and a devaluation of depositors needs are all results of amalgamation, but the local economy has been substantively unaffected. It appears the growth of financial services in general and changes in the banking organizations doing business locally will continue to contribute to the overall growth of San Diego’s economy.

397. See SELECTED ECONOMIC INDICATORS, supra note 387.
398. FUTURE SCAN, supra note 246, at 27.
399. Id.
2. Have There Been Increased Employment Opportunities in San Diego as a Result of this Extreme Amalgamation?

At one time the government was the largest employer in San Diego County; today, the services and retail market far outrank the military, and soon the agricultural business will also. Still, San Diego is home port to over 90 military ships. In 1987, approximately 1,011,000 people were employed in San Diego County, by year-end 1998 that number is forecasted to be 1,232,000, a growth of over 200,000 in employees in just over ten years. The strength of the region's economy is revealed by San Diego's relatively low unemployment rate.

Unemployment rates for most ethnic groups in the region tend to be higher than the unemployment rate for Caucasians. Estimated unemployment rates by ethnic group were: Caucasians, 4%; blacks [African-Americans], 8%; Hispanics, 6%; Asian/Pacific Islanders, 4%; American Indians, 8%; and Other, 7%. The youth unemployment rate in the San Diego region [was in 1989] estimated to be 16%, compared to a [1989] national rate of approximately 25%. Unemployment rates for most ethnic youth also tend to be higher than the rate for Caucasian youth. Unemployment rates among the region's black [African-American] and Hispanic youth [were] estimated [in 1989] to be as high as 36% and 24%, respectively.

San Diego's work force is composed of a higher number of women and ethnic groups than ever before. Still the county's unemployment rate is expected to remain lower than forecasted rates for the state of California and the nation.

Hostile takeovers often bring job layoffs or severe reductions in worker compensation to companies targeted for acquisition. At an individual company, the acquisition process may eliminate a significant portion of the workforce. Such was certainly the case during the San Diego Trust, First Interstate, BankAmerica, and Wells Fargo mergers. The Great American and Home Federal preliminary layoffs could be attributed to amalgamation, but the final layoffs could perhaps be more directly attributed to capitalization problems than the final merger activities of the two institutions. Conversely, these same final mergers caused immediate and long-reaching capitalization failures that led to their demise.

At year-end December 31, 1986, one of its most successful years, Great American employed 3,394 people and considered its employee relations to be excellent. At its demise in 1992, the number of Great American em-

401. See SELECTED ECONOMIC INDICATORS, supra note 387.
402. FUTURE SCAN, supra note 246, at 28.
403. See id.
ployees had trickled down to 187. Many financial institution employees were assisted with outplacement, but an estimated 1,200 remained out of the workforce for a significant period of time. Still, San Diego County was expected to add 30,000 new jobs to its workforce in 1998, a 3% increase over 1997.

On December 31, 1986, after Wells Fargo’s acquisition of Crocker National Bank, Wells reported a total of 21,500 employees, a 54% increase in the number of Wells employees at year-end 1985. As part of the Crocker Merger, Wells Fargo fired 4,000 people. Of that number only 620 were employed at operations in San Diego County. By the time of the next major Wells Fargo deal in the San Diego area, the purchase of the Great American retail branch network, Wells had reduced its employees in San Diego county to approximately 300. Combined Wells Fargo and Great American employees in the San Diego area by year-end 1991 totaled 2,500.

This suggests that between 1986 and 1992, an estimated 2,900 Crocker, Great American, and Wells Fargo employees in the San Diego area were terminated or outplaced in some manner. The more amalgamation activity, downsizing, and bank failures, the greater the tendency to also use contract and part-time workers. “Three thousand San Diego jobs were lost in 1990 alone as a result of the failure of Imperial Savings Association.”

Four thousand jobs vanished when the First Interstate merger swallowed up San Diego Trust. The effect these employment changes had on the San Diego community was profound. During this same time period the San Diego aerospace industry suffered a large decline, but the services industry experienced phenomenal growth.

Industry executives seemed to think that layoffs would be minimal in the 1996 merger rush for Great Western. Employment effects were consid-

405. See Telephone Interview with Dan Conway, Public Relations Officer, Wells Fargo Bank (Apr. 27, 1998).
406. See id.
407. See SELECTED ECONOMIC INDICATORS, supra note 387.
409. See id.
411. See id.
412. See id.
413. Id. At the “end of the Second Quarter of 1987 [June 30, 1987] Imperial Savings was ranked the third largest San Diego area savings institution, with $10.1 billion in total assets, approximately $5.6 billion total deposits, and $3 billion in loans. The company’s net worth was $215,512 million. At that time, Imperial had 3,000 employees and 15 branch offices in San Diego County.” Id. See also Top S&Ls, SAN DIEGO BUS. J. BOOK OF LISTS, Dec. 1987, at 79. But, on February 23, 1990, the Office of Thrift Supervision seized Imperial Savings. See generally STATISTICS ON BANKING, supra note 3.
erected a plus factor for one of the possible suitors, NationsBank, because the operations of the two institutions would not overlap; however, since the victor, Washington Mutual, completed the merger in March 1997, 2,290 Great Western and Keystone employees have been casualties.415 Pursuant to a restructuring plan, the resulting number of Washington Mutual employees declined by 1,737 full time employees by December 1997, to 19,880 total Washington Mutual employees.446 An additional 1,190 employee separations were planned for completion by the end of June 1998.447

During 1996, Ahmanson made a hostile takeover bid for Great Western. It was expected that if the Ahmanson hostile deal had been successful, the lion’s share of layoffs would of course come from Great Western employees rather than what would be the newly combined pool of both Ahmanson and Great Western employees. As of June 30, 1997, Great Western had a labor force of 12,000 employees,448 approximately 500 in San Diego County alone. In March 1997, Great Western agreed to be acquired by Washington Mutual, certainly a decision in no small way effected by the plight of Great Western employees. In connection with the Great Western merger, Washington Mutual recorded transaction-related expenses of $431.1 million in 1997.419 The largest of these expenses were in the category of severance and management payments and other direct transition costs.420 Great Western originally had over 1,000 mortgage lending, retail banking, and consumer finance offices operating in twenty-three states.421 Washington Mutual planned to close ninety of these offices by the third quarter of 1998.422

Wells Fargo completed its purchase of the entire retail branch operations of Great American on August 1, 1991, displacing 200 of the remaining Great American employees in the months immediately preceding and following the purchase.423

Bank of America merged with Security Pacific National Bank in 1992, the Bank of America Merger Transition Program is attributed with saving the jobs of approximately 1,100 Security Pacific and Bank of America employees.424 However, a large number of employees were terminated, accepted severance packages, or elected premature retirement between 1991 and


416. See id. at 34.

417. See id. at 35.


420. See id.

421. See id. at 27.

422. See id. at 35.


424. See Parker v. BankAmerica Corp., 50 F.3d 757, 761-62 (9th Cir. 1995).
First Interstate Bank of California acquired San Diego Trust & Savings Bank in 1994. The acquisition brought the number of First Interstate employees in the San Diego area to 1,900. When Wells Fargo completed its merger with First Interstate Bank of California during 1996, and closed forty San Diego First Interstate branches while divesting itself of ten more, several hundred of the combined employees of San Diego Trust and First Interstate were affected. A total of 12,000 jobs were eliminated as a result of the $11.3 billion merger between Wells Fargo and First Interstate.426 "A significant portion of the decrease [in Wells Fargo’s 1997 fourth quarter noninterest expense] was related to reduced salaries, incentive compensation and employee benefits due to staff reductions after the merger with First Interstate Bancorp."427 As some indication of the total number of First Interstate and Wells Fargo employees affected by this merger, note that Wells Fargo disclosed an estimated $270 million restructuring charge/severance cost to be incurred in connection with this merger.428 Today, San Diego area Wells Fargo employees total 2,000.429

[During 1993], Bank of America... asked all employees to sign 'at will' statements acknowledging that the bank may fire them without cause at the employer’s pleasure, work hours may be cut and health care and other benefits taken away, and employees may be transferred anywhere in the bank’s system; [this kind of] personnel action compromises the principle of employer responsibility by implying that the cutting of employee hours, salaries and benefits is acceptable behavior while the bank continues to earn large profits; the elimination of employee benefits by [Bank of America] may place an additional burden on the state budget by increasing the costs of the Medi-Cal system and of state hospitals for uncompensated care.430

A reduction in employment sometimes comes into focus as a result of the accompanying scrutiny of merger activities. Bank of America, known as the leading bank in the West and one of the most profitable financial institutions in America, made a profit of $1.5 billion in 1992; the bank had achieved this success in part through federal subsidies of FDIC guaranteed borrowing and mergers approved by the federal government.431 California House Resolution 20 (HR20) chastised Bank of America’s Chief Executive Officer’s salary of $1.6 million in 1992 and his exercise of approximately

426. See Murray, supra note 409, at A2.
429. See Telephone Interview with Dan Conway, Vice President of Public Relations, Wells Fargo Bank (Apr. 27, 1998).
431. See id. (citing California House Resolution 20 (1993)).
$12 million in stock options between 1987 and 1991, as well as the bank’s opening of overseas offices in Vietnam while at the same time closing neighborhood banks in California communities.\textsuperscript{492} Further, citing Bank of America’s decision to move its credit card operations to Arizona, transferring 1600 jobs out of San Francisco and Glendale in order to escape California consumer protection laws,\textsuperscript{493} and Bank of America’s banking dominance in the state of California,\textsuperscript{494} HR20 author Representative Burton recommended a complete divestiture by the State Treasurer and state agencies from Bank of America, “in accordance with ordinary care, prudence, skill and diligence that a prudent person would use in conducting or making state financial investments.”\textsuperscript{495}

If the type of actions and ethics commented upon by HR20’s author are embraced by a financial institution partially to maximize the implications of the merger activity in which the bank has participated, how could California in general, and San Diego particularly, possibly expect local employment in any way to be positively impacted by amalgamation?

Perhaps partially as a result of negative public discussion of Bank of America’s employee relations, prior to the Security Pacific merger, the bank created a Merger Transition Program (MTP), a severance program for bank employees whose positions were eliminated or displaced by merger or consolidation.\textsuperscript{496} MTP provided:

- "Transition assistance which included Program pay, including severance pay; Outplacement assistance, Continuation/extension of certain benefits; Special treatment of stock based benefits; AND Additional special benefits.” Thus, the MTP provide[d] discrete benefits for former employees who were guaranteed and received continuous employment, without interruption, ... after [a] divestiture, and for the displaced employees. Under the MTP, divested employees are entitled to appropriate positions with [the entity acquiring the sold BankAmerica business unit.] If a divested employee did not receive an appropriate position, that employee [was] eligible for benefits under the MTP. In contrast, displaced employees were entitled to transition benefits upon being notified that their employment would be terminated.\textsuperscript{497}

MTP packages were expensive, however, and were not used with notable discretion. As a result, several lawsuits were filed by employees and former

\textsuperscript{432} See id.

\textsuperscript{433} These consumer protection laws do not apply if the credit card business is headquartered in a state with weaker regulations. See id.

\textsuperscript{434} As the depository bank for the State of California, 91% of all deposits from California state agencies are deposited with BofA, during the 1991-92 fiscal year the State of California’s total dollar investment in BofA of $3.9 billion, and the State of California’s $131 million in debt issuance corporate notes from the Pooled Money Account were with the BofA. See id.

\textsuperscript{435} Id. See also Cal. Pub. Law 95-129-8 (1985).

\textsuperscript{436} See Parker v. BankAmerica Corp., 50 F.3d 757, 761-62 (9th Cir. 1995).

\textsuperscript{437} Id. at 761.
employees of Bank of America and Security Pacific in connection with what was perceived as discriminatory practices via unfair application of the MTP.438

3. Have the Community Reinvestment Activities of the Remaining San Diego Financial Institutions Been Affected by Amalgamation?

Adopted by Congress in 1977, the Community Reinvestment Act (CRA)439 became effective November 6, 1978. Since then it has become known for a longstanding history of inspiring compliance and service to the communities in which branches of either a savings institution or bank operate. "[T]he CRA is designed to promote affirmative and ongoing efforts by regulated financial institutions to help meet the credit needs of their entire communities ... consistent with safe and sound operations."440 Under CRA, banks and other depository institutions are required to meet the credit needs of the entire community in which they operate, including low- and moderate-income neighborhoods. CRA performance by banking organizations must be taken into account by regulatory authorities in judging expansion applications.

During the 1980s, savings institutions, especially in the San Diego area, appeared to take great pride in their CRA service to the community. Several of the San Diego savings institutions were not only headquartered in San Diego, but were originally owned by founding citizens of the city and managed for decades by their descendants. This was true of Home Federal, Great American Bank, and San Diego Trust. Annually, Great American issued a CRA Statement and, in May 1989, even published a detailed, expansive, and cumulative account of their own community reinvestment service throughout San Diego County, Los Angeles, and the communities in which they operated in Arizona, Montana, Washington and Colorado.441 Home Federal and San Diego Trust regularly released to the public their own record of CRA activities in the city of San Diego. CRA accomplishments still appear to be a source of pride for all locally based banking organizations.

In the late 1980s and early 1990s, the Federal Home Loan Bank of San Francisco operated a Community Investment Fund (CIF) Program which encouraged participant banks and savings institutions to extend reduced rate home loans to mortgage deficient (defined as low/moderate income and minority) areas throughout the State of California.442 Under the CIF loan program, home loans were made at twenty basis points below the interest rate

---

440. Lebrecht, supra note 430, at 93.
442. See id. at 13.
on current loan rates. In 1988, Great American reported making over $22 million loans under this program.\textsuperscript{443}

During this time at the state level, an organization called the California Equity Fund, a subsidiary of the Local Initiatives Support Corporation, operated a program to create affordable housing in local neighborhoods throughout California.\textsuperscript{444} In 1988, Great American contributed $1 million to the California Equity Fund.\textsuperscript{445} Between 1991 and 1995, BankAmerica became one of the largest investors in the Local Initiatives Support Corporation (which is a national nonprofit group that provides equity financing for affordable housing under the federal Low Income Housing Tax Credit Program).\textsuperscript{446}

San Diego Trust and Savings Bank saw itself as a leading San Diego corporate citizen and, as such, claimed to support over 250 community organizations.\textsuperscript{447} This bank actively encouraged its employees to contribute volunteer hours and make monetary donations to the community organizations of their choice.

However, application of CRA standards were not consistently applied and enforced by the financial regulatory agencies or by the financial institutions themselves.

[Thus, in July 1993,] President Clinton asked the four major banking regulatory agencies... to work together to “reform the Community Reinvestment Act enforcement system... [to] replace paperwork and uncertainty with greater performance, clarity, and objectivity.”... [The four agencies held six public hearings around the country to obtain public input on improving federal enforcement of the CRA...\textsuperscript{448}]

In December 1993, the Office of the Comptroller of the Currency (OCC), the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision proposed new regulations to implement the federal Community Reinvestment Act (CRA). [The proposed regulations would replace the existing CRA regulations in their entirety. The continuing purpose of the CRA being to promote the] affirmative obligation of regulated financial institutions to help meet the credit needs of their communities... consistent with safe and sound operations; the proposed regulations are intended to provide guidance on how the agencies assess the performance of institutions in meeting that obligation. In response to the initial rule-making proposal, the agencies received over 6,700 comments, which they spent ten months reviewing.

On October 7, [1994,] the four agencies published a revised rule-making proposal... [to] provide guidance to financial institutions on the nature and extent of their CRA obligation and the methods by which that

\textsuperscript{443} See id.
\textsuperscript{444} See id.
\textsuperscript{445} See id.
\textsuperscript{448} Lebrecht, \textit{supra} note 430, at 93.
obligation will be assessed and enforced, emphasize performance rather than process, promote consistency in assessments, permit more effective enforcement against institutions with poor performance, and reduce unnecessary compliance burden while stimulating improved performance. As compared to the December 1993 proposal, the agencies contended that the revised proposal broadens the examination of performance, more explicitly considers community development activities, and makes other modifications and clarifications.

[T]he revised proposal . . . eliminate[d] the existing regulation's twelve assessment factors and substitute[d] a performance-based evaluation system. . . . [It also made] explicit the assessment context against which the tests and standards set out in the proposed regulations would be applied, including consideration of demographic data about the community, information about community characteristics and needs, . . . information about the institution's product offerings and business strategy, data on the prior performance of the institution, and data on the performance of similarly-situated lenders. [This proposal gave] particular attention to an institution's record of helping to meet credit needs in low- and moderate-income geographies . . . and individuals where appropriate, given community characteristics and needs. The revised proposal retain[ed] the lending, service, and investment tests as the primary method by which the agencies will assess . . . CRA performance . . . .

In addition to this rulemaking, the agencies proposed to work together "to improve examiner training and to increase interagency coordination regarding application of standards, performance of examinations, assignment of ratings, and use of enforcement tools. The agencies are also committed to work together to improve public access to data collected pursuant to the Home Mortgage Disclosure Act [HMDA]."449 "HMDA is a 1975 law that requires banks and other depository institutions to compile and make available to the public and supervisory authorities information about home mortgage and home improvement lending practices."450 According to the agencies, these efforts "should produce a CRA assessment process that is less burdensome for many institutions and yields more results for the local communities the law is intended to benefit."451 "Within days of the release of the proposed rules, banking industry trade associations began to voice opposition to various elements of the plan."452 There were issues with the proposed loan-to-deposit ratio for smaller banks because of the feeling that in order to meet the suggested lending ratio, banks may feel forced to engage in risky lending practices.453

The California State Banking Department administers all laws applica-

449. Brenot, supra note 39, at 102-03.
450. Lebrecht, supra note 430, at 93.
452. Lebrecht, supra note 430, at 93.
453. Id.
454. See id.
ble to corporations engaging in commercial banking, including those regulating the establishment, operation, relocation, and discontinuance of various types of offices of these entities.\footnote{55} As part of this administrative duty, the chief officer of the Department, the superintendent, must consider and decide what the implications of these matters will be on the CRA.\footnote{56} The Department coordinates its examinations with the FDIC so that every year each agency examines certain licensees.\footnote{57}

At the state level, the California State Banking Department recommended a further redraft of the revised CRA proposal of the four key federal agencies because of its concerns that: the new data collection and reporting requirements were onerous; the tests were vague and could be implemented inconsistently; the statutory authority may not exist for proposing sanctions, such as civil money penalties and cease and desist orders; and finally, that such proposed sanctions could encourage banks to ignore safety and soundness for the sake of compliance with the regulations.\footnote{58} Even the Consumer Federation of America joined the criticism of the revised CRA proposal by their contention that it failed to give proper weight to a bank’s record of providing branch and deposit service in low-income and minority neighborhoods, citing the provision of deposit services as both a very basic and general obligation under the CRA, and a critical aspect of meeting both the convenience and community needs of these communities.\footnote{59} The Consumer Federation’s position was that the regulatory agencies must support revisions which provide that no bank may receive a passing composite rating unless it earns a satisfactory or better score under the service test for delivering complete deposit-side services.\footnote{60} These services should be measured for success by whether there is an increase or decrease in new accounts in low-income and minority neighborhoods.\footnote{61}

On occasion, without competitor or community intervention, the Federal Reserve Board has, on its own initiative, raised the matter of Community Reinvestment Act records of institutions seeking approval for merger or acquisitions.\footnote{62} At least one institution, perceived by the Federal Reserve as needing improvement in this area, responded to the Board’s concerns by submitting a new plan found acceptable by the Board.\footnote{63} The plan required the bank to submit semi-annual reports updating the Board on promises made by the plan, including:

\footnotesize{455. See CAL. FIN. CODE § 100(a) (West 1989 & Supp. 1998).}
\footnotesize{456. See Lebrecht, supra note 430, at 93; CAL. FIN. CODE § 4886(g) (West 1989 & Supp. 1998).}
\footnotesize{457. See CAL. FIN. CODE § 4886(g) (West 1989 & Supp. 1998).}
\footnotesize{458. See Brenot, supra note 39, at 103.}
\footnotesize{459. See id.}
\footnotesize{460. See id.}
\footnotesize{461. See id.}
\footnotesize{462. See Capital, CRA Issues Dominate Recent Board Decisions, 7 No. 16 BANKING EXPANSION REP., Aug. 15, 1988.}
\footnotesize{463. See id.}
With regard to "Banking Services," ... [the bank] will:
- promote services to its communities through regular product advertising in mass media newspapers and locally targeted publications, and through special advertising programs;
- develop employee understanding and awareness through written communications, formal training, internal publications and quarterly review meetings;
- ascertain community needs through a "grassroots" outreach program which will be developed by an experienced individual;
- evaluate existing products and address changing needs through analysis of market penetration by product and review of consumer and small business lending activity;
- develop and introduce new products such as credit cards, student loans, subsidized loans, and small business loans and deposit accounts; and
- evaluate services offered and address changing needs through a market research project and a program for the hearing impaired.

With regard to "Housing Services," [the bank] will:
- promote existing mortgage products through traditional and special advertising programs;
- ascertain community needs through work with [community/city] housing offices;
- evaluate products and address changing needs through analysis of mortgage applications, approved and denied by census tract, review investments in government housing related securities, ... making available adjustable rate mortgages and no income check mortgages;
- participate in housing development and redevelopment programs; and
- make funds available for participation in rehabilitation projects and mortgage loans.

With regard to "CRA Compliance," [the bank] will:
- Revise its CRA statement as needed;
- review and revise community delineations, as needed;
- provide employee training on CRA;
- evaluate CRA compliance;
- document CRA compliance; and
- revise its community action program. 464

Despite CRA's notable successes, bank and thrift industry, community, consumer, and other groups maintain that its full potential has not been realized because, in large part, compliance efforts have focused on process at the expense of performance. 465

Along with federal and state antitrust laws that apply to interstate banking, the Federal Reserve Board must also consider Community Reinvestment Act compliance in connection with any merger or acquisition application. For example, in its analysis of the antitrust concerns and of a CRA protest of Security Pacific National Bank's acquisition, the Federal Reserve Board found "the convenience and needs considerations in this case were consistent with approval of Security Pacific National Bank's acquisition application." 466

464. Id. at 28-29.
465. Lebrecht, supra note 430, at 93.
466. Application in connection with the acquisition of American Asian Bancorp, San
The Board did an analysis of both applicant financial institution’s CRA records, the CRA compliance of all Security Pacific’s subsidiaries, and Home Mortgage Disclosure Act data for the years and the geographic area in question and concluded there existed no pattern of discrimination against minority and low-income neighborhoods.467

Security Pacific held a meeting to discuss the establishment of a working group within the bank to increase its CRA program coordination and to establish system-wide CRA compliance and reporting programs. The Board cited Security Pacific’s involvement with organizations that identify the needs of low- and moderate-income persons and develop and manage programs that address those needs. Further, the Board found Security Pacific placed advertisements in local publications targeted to low- and moderate-income persons and practiced some flexibility in its underwriting criteria and loan application procedures.468

A community organization in California also protested the First Interstate merger with San Diego Trust and Savings Bank. The protest charged that both institutions “failed to meet the credit needs of minorities and low- and moderate-income individuals in the San Diego area,” and that “the merger would reduce the credit products available to the San Diego community.”469 The Federal Reserve Board rejected this complaint based on 1) First Interstate having received “outstanding” or “satisfactory” CRA performance ratings from regulators during its most recent examinations, 2) First Interstate-California’s offering a variety of relevant loan products, including a down payment assistance program to make home ownership more affordable, and 3) First Interstate’s commitment of $7.8 million in construction and permanent financing for a 53-unit, single-family residential housing project in a predominately minority, low- and moderate-income area of San Diego.470 In addition, the Board recognized First Interstate’s support of the California Community Reinvestment Corporation in financing a rent-controlled housing project in San Diego.471

Through the years there have been consistent attempts in California State government to encourage financial institution compliance with the CRA. California Assembly Bill 1756, which died in committee during 1994, would have prohibited state, city and county governments from contracting for services with financial institutions with $100 million dollars or more in assets unless those companies file Community Reinvestment Act reports annually with the [State] Treasurer.


467. See id.

468. See id.

469. 12 First Quarter Actions Include Okay of Deal Once Denied Under CRA, 13 No. 8 BANKING POL’Y REP. 12, 13 (Apr. 18, 1994).

470. See id.

471. See id.
would have been required to annually submit a report to the legislature and to make summaries available to the public. These reports would have included specified information regarding the nature of the governance of the companies, and their lending and investment practices, with regard to race, ethnicity, gender, and income of the governing boards and of the recipients of loans and contracts from the institutions.472

What better way would there ever be to determine if California banks had in fact or were attempting to meet the credit needs of the entire communities in which they operated, especially the low and moderate income neighborhoods? Yet as late as 1995 the California political climate would not support such a bill.

In 1998, with local savings institutions nearly extinct, community reinvestment in San Diego by the major market banks is tremendously different. Washington Mutual made a point of emphasizing its reputation for community giving during and after the Great Western merger, citing its activities "through grants, volunteer time, in-kind services and other support, the company strives to give back 2% of its pre-tax earnings to the communities where it does business. This equates to over $10 million in grants, services and volunteer time given back to the community."473 Also, in connection with the Great Western merger, Washington Mutual pledged $75 million to CRA activities in the communities in which it does business.474

Wells Fargo made a $45 billion, ten-year community reinvestment commitment in connection with the acquisition of First Interstate Bancorp.475 Two and one half years into the pledge, the bank reports a $16 billion accomplishment in CRA lending.476 As of June 30, 1998, Wells Fargo has made $213 million in community investment commitments toward its $500 million, ten year CRA investment goal and $300 million in corporate contributions to the communities in which the bank conducts business.477

BankAmerica reports earning three consecutive Community Reinvestment Act ratings of "Outstanding."478 Through its Bank of America Community Development Bank, it provides affordable low-to-moderate income housing in over 40 states.479 The bank committed $140 billion to community development lending over ten years, the largest goal set by a bank.480 During 1998 a new branch, staffed by tribe members, was opened on an Arizona In-
If there is a weakness in the bank’s community relations it is among its own workforce. BankAmerica has long been known for lagging behind other banking organizations in the areas of hiring, promoting, and valuing diversity in its own employees. This perception is being addressed by a program to train 12,000 of its middle management staff on diversity in the workplace, having already trained 20,000 in this area in recent years.\textsuperscript{41}

Union Bank has devised and published an annual plan specifically addressing its Community Reinvestment activities since 1988, as well as a Community Reinvestment Act Statement reporting the results achieved in connection with the plan, each year. The first sentence of the 1988 plan (originally a California First Bank publication) acknowledges the bank’s awareness of its “responsibility as a corporate citizen in the communities it serves.”\textsuperscript{42} It lists those responsibilities as “the provision of credit and deposit services to Californians of low and moderate income; cash contributions to non-profit community organizations, assistance to local governments in financing public projects, and the involvement of local employees in community service. Furthermore the Bank recognizes that it will, as a result of its pending merger with Union Bank, accept a greater responsibility to help meet the financial needs of the community.”\textsuperscript{43} This approach, while it simply communicates the underlying theme of community reinvestment in general, is certainly novel to make such a statement so immediately and emphatically. Certainly the conglomerate banks of today have begun to directly approach the issue of corporate responsibility.

Union Bank’s results have been significant. The bank has consistently met or exceeded its set lending goals. The bank exceeded the 1988 lending goal of $84 million, reached its goal of $148 million in lending for 1991-1992, and set a community-lending goal of $184 million in the 1993-1994 plan.\textsuperscript{44}

The locally based small banking organizations also uphold their CRA responsibilities. In fact, several “local” banks have earned “Outstanding” CRA ratings consistently.\textsuperscript{45}

In 1940 it was said:

\textquote{The big banks are the leaders in the savings-bank field. They are not always followed, but they set the pace. They have done little to clean out the slums. They have overbuilt Park Avenue. They have shown no leadership toward a social use of the funds they guard...[or the] great power they have...[b]ut of what use is this power to their city, to the state or to the nation? They cannot be trusted adequately to represent such power, nor...}
can any surrogate for them do so. Power corrupts the user. It blinds his vi-
sion. It deprives him of kinship with the lowly. Holding in his hands the
right to vote a half billion dollars, he soon fails to feel the essence of his
power—the $800 deposited on the average by each of the depositors in his
bank. 486

Some truth still rings in this statement today; if it did not, we would not need
four regulatory agencies to lord over the business of bank amalgamation.

The time is long past when challenges to bank mergers and acquisitions,
targeted against transactions involving large institutions and coming princi-
pally from community interest groups, only involve claims of inadequate
compliance with CRA or fair lending laws. 487 There remains a high per-
centage of CRA protests; however in late 1996, a trend of attacking banking and
product expansion applications on much broader grounds began. 488 During
the third quarter of 1997, protests raised by both competitor organizations
and community interest groups have been more broadly-based on concerns
about managerial resources; adverse competitive effects on markets served
by existing financial institutions; concentration of banking resources; discrimi-


486. ERNST, supra note 15, at 110.
487. See Wide-Ranging Protests Target Third Quarter Applications of All Kinds, 16 No.
22 BANKING POL'Y REP. 10 (Nov. 17, 1997).
488. See id.
489. See id. at 10-12.
490. See id. at 11. Well into 1997, the strategy by activist and community coalitions was
to continue these new lines of attack on banking expansion. These coalitions questioned many
other issues such as capital adequacy considerations, state deposit caps, a bank subsidiary’s
relocation of its main office, the competitive effects of automated teller machine (ATM) sur-
charges on both customers and non-customers, problems with ATM services, billing errors
with secured credit cards, management competence, the departure of mid- and high-level
management executives, the effectiveness of boards of directors, Department of Labor re-
views of a bank’s labor practices, incidents of alleged employment discrimination, branch
closing practices, trading in unregistered futures, mutual fund sales practices, minority in-
vestment in the applicant bank, the reliability of data submitted under the Home Mortgage
Disclosure Act, and even a bank’s luxury auto lending practices that allegedly excluded low-
and moderate-income and minority borrowers. See Activists Are Challenging Bank Expansion
on Much More than CRA Performance, 16 No. 3 BANKING POL'Y REP. 7, 7-10 (Feb. 3, 1997).
491. See id. (reorganization of Chemical Bank by Chase Manhattan).
business in San Diego remain very conscious of their CRA responsibilities. Most still publish annual CRA statements that highlight their achievements even though federal law passed in 1997 no longer requires them to publish this data publicly. Financial institutions never know if or when inattentiveness to CRA matters will affect their next amalgamation plan.

4. Have the Needs of Small San Diego Businesses Been Negatively Impacted as a Result of Amalgamation?

On September 29, 1994, the governor of California signed into law Assembly Bill 2233 which directed “the California Research Bureau of the California State Library to conduct a study of factors affecting credit for small businesses, including the effect of state and federal financial institution laws and regulations on small business loans and report to the legislature by July 1995.” The problems of small businesses in California are of utmost importance to its economy because the majority of employers and contributors to the gross regional product in each California county are small businesses.

San Diego has a “small business” character that continues to increase. Its myriad of major educational centers, biomedical research, and genetic engineering has become an “incubator” for emerging companies in the high-tech field and entrepreneurs who convert research findings into marketable products. San Diego is now the nation’s fourth largest center for the bio-tech industry. The County’s bioscience employment in 1996 numbered 21,290, an 8.5% increase over 1995.

The “start up” companies of the late 1980s will become the mid-sized and large corporations in the years ahead. “Of the estimated 64,000 businesses [in 1989] in San Diego County, 95% employ fewer than 50 persons, with 75% of these companies employing fewer than 10 persons. Approximately 700 companies employ[ed] 100 or more persons.” San Diego statistics now report 70% of San Diego companies qualify as small businesses. In 1995, there were 76,727 small businesses with ten or less employees and 12,248 small businesses with 11 to 50 employees. These 88,975 small San Diego businesses employ 534,024 of the total San Diego

492. Those seven are BankAmerica, Wells Fargo, Union Bank, Grossmont Bank, Washington Mutual, Scripps Bank, and Peninsula Bank.

493. Brenot & D’Angelo, supra note 154, at 114.


495. See id.

496. FUTURE SCAN, supra note 246, at 31.

497. See id. “Small Businesses” are defined in this study as “those businesses employing less than 50 employees.” Id.

498. See SAN DIEGO ASSOCIATION OF GOVERNMENTS (SANDAG), POPULATION AND ECONOMIC CHARACTERISTICS (SAN DIEGO REGION) 3 (1995).
workforce of 1,091,190, or 49% of San Diego’s total employment.499

San Diego is still the largest county in the country for military and civilian salaries/wages by the Department of Defense. For the year-ended December 31, 1996, the San Diego County payroll for military/civilian wages was $3,658,889.500 “The defense industry accounted for 12% of San Diego’s gross regional product (estimated to be $79 billion in 1996). Only manufacturing has a greater impact on the local economy, although some defense revenues are also counted as manufacturing.”501 In “1996 San Diego was home port to 96 Navy ships, including two aircraft carriers,” with active-duty naval personnel totaling 67,400, down from over 94,000 in recent years.502 Marines based in San Diego increased to 45,740.503 “San Diego is home to the largest number of military retirees anywhere in the nation.”504 Over 260,000 military veterans, receiving $953 million in retirement compensation, live in San Diego.505

High technology employment in San Diego rose 18.2% to 104,250 in 1998, and is on a pace to double within five years.506 There were 16,310 new jobs added by high-tech companies during 1997, “accounting for 36% of all new jobs created in San Diego during the year.”507 The San Diego computer and office equipment industry alone employed 15,722 San Diegans as of year-end 1996, in the manufacturing of component parts and software development and design, and includes thirty seven companies.508 “The end of the Cold War brought an almost total collapse of San Diego’s defense industry during the early 90’s. Aerospace and defense had dominated local economic activity for at least the past fifty years. The downsizing of defense brought on and prolonged the longest and deepest recession in the area since the Great Depression of the 1930’s. Two of every three aerospace and defense jobs existing in San Diego... vanished, falling from 44,000 in 1990 to fewer than 15,000 by 1996.”509

Tourism is the heart of many small businesses in San Diego. The num-

499. See id.
500. See GREATER SAN DIEGO CHAMBER OF COMMERCE, ECONOMIC BULLETIN 1, 2 (Aug 1997).
501. Id.
502. Id.
503. See id. at 3.
504. Id.
505. See id. at 7.
506. See GREATER SAN DIEGO CHAMBER OF COMMERCE, ECONOMIC BULLETIN 1 (Sept. 1998).
507. Id.
ber of visitors to San Diego has increased each year since 1987.510 Approximately 13.9 million tourists came to San Diego in 1996 and contributed approximately $4 billion to its economy.511 On December 31, 1996, tourism supported 125,300 jobs in the county.512 “Visitor revenues represent San Diego’s third largest [industry, with] visitor spending account[ing] for 5.1 percent of San Diego’s 1996 gross regional product (GRP), estimated to be $79.1 billion.”513 San Diego small businesses receive billions of dollars in defense contracts for shipbuilding, military facility maintenance, aircraft, missile, aerospace, and avionics work each year. In addition, the defense industry significantly contributes to San Diego small business income. Total defense-related spending was estimated to have a $17 billion impact on San Diego’s economy during 1996.514

The lending policies of the major commercial banks that now predominate in San Diego are not supportive of small businesses. For example,

James Worrell [owner of a small heating and air conditioning company] says the banking industry’s wave of mergers left his business treading water.

After National Westminster Bank PLC in 1995 acquired the lender [Worrell’s] business used, [he] tried to increase his $15,000 credit line. Instead, the bank cut the credit line by one-third.

. . . .

After mergers, “there are always people... who for any number of reasons have their credit scaled back,” says Joseph Wessley, an executive vice president at Boston’s Fleet Financial Group Inc . . . .

. . . .

Many small business owners like Mr. Worrell worry that they will lose out after mergers. Now, a Wall Street Journal computer analysis of federal banking reports suggests that their fears are justified. The Journal examined the five biggest bank holding company acquisitions and mergers completed at least a year ago. In every case, small business’s share of the companies’ combined business-loan portfolios declined. The drop represents $1.9 billion in loans that small businesses didn’t get.

Overall the small-business loan portfolios of the merged bank holding companies fell 6% while their total business loan portfolios grew slightly. By contrast, the small business portfolios of the six biggest holding companies that did not go through major mergers rose 7.5% during the same period. All but one of those companies increased small businesses’ share of their business-loan portfolios.

510. See id. at 4-5.
511. See id. at 4.
512. See id.
513. Id.
514. See id. at 1, 2.
... At Fleet, whose small business loan portfolio declined the most among the merged companies, nearly a third of the drop stemmed from divestitures required by regulators for antitrust reasons.515

Although nationally small business loans tend to decline after a merger, in recent years, SBA loans made in San Diego County by local commercial banks have rebounded. For the period of October 1, 1997, through September 30, 1998, Union Bank made thirty-three SBA 504 loans totalling $24,486,050.516 These loans are guaranteed by the SBA and provide 90% financing to small businesses who are buying or building commercial properties.517 Grossmont Bank made eleven 504 loans for a total loan amount of $8,875,750 in San Diego, Riverside, Orange, and Los Angeles counties.518 Others making 504 loans included:519

<table>
<thead>
<tr>
<th>Banks Making 504 Loans</th>
<th>No. of 504 Loans</th>
<th>Total of Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>BankAmerica Community Development Bank</td>
<td>16</td>
<td>$8,039,000</td>
</tr>
<tr>
<td>Scripps Bank</td>
<td>14</td>
<td>$7,099,258</td>
</tr>
<tr>
<td>Wells Fargo Bank</td>
<td>12</td>
<td>$6,517,500</td>
</tr>
<tr>
<td>Peninsula Bank</td>
<td>4</td>
<td>$3,907,250</td>
</tr>
<tr>
<td>Bank of Commerce</td>
<td>7</td>
<td>$3,500,473</td>
</tr>
<tr>
<td>First National Bank</td>
<td>1</td>
<td>$1,050,000</td>
</tr>
<tr>
<td>San Diego National Bank</td>
<td>1</td>
<td>$252,000</td>
</tr>
</tbody>
</table>

In addition to 504 loans, the BankAmerica Community Development Bank also made eighty-four SBA 7A loans in San Diego County from October 1, 1997, through September 30, 1998, totaling $6 million.520 In that same period, Bank of Commerce made fifty-three 7A loans totaling $22 million; however, only a portion of these loans were made in California generally.521

---

517. See id.
518. See id.
519. See id.
520. See id. at 18. These 7A loans are guaranteed by SBA and are for the general business needs of qualifying businesses, such as debt refinance, real estate, inventory, equipment, and company acquisitions. See id.
521. See id.
Other lenders under 7A included:  

<table>
<thead>
<tr>
<th>Banks Making 7A Loans</th>
<th>No. of 7A Loans</th>
<th>Total of Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scripps Bank</td>
<td>50</td>
<td>$9,000,000</td>
</tr>
<tr>
<td>Pacific Commerce Bank</td>
<td>24</td>
<td>$4,000,000</td>
</tr>
<tr>
<td>Peninsula Bank</td>
<td>20</td>
<td>$3,000,000</td>
</tr>
<tr>
<td>Grossmont Bank</td>
<td>17</td>
<td>$4,000,000</td>
</tr>
</tbody>
</table>

In conjunction with the Great Western merger, in April 1997 Washington Mutual announced a commitment to make $9 million in small business loans of $50,000 or less over a ten year period. In comparison, in 1993 Union Bank announced a plan to extend $110 million in small business loans and lines of credit to non-profit community organizations. Four full-time SBA specialists in Northern California, Los Angeles, Fresno, and San Diego administer Union Bank’s plan.

At the time of the Crocker acquisition by Wells Fargo, Crocker had demonstrated a virtually unmatched commitment to small businesses and entrepreneurial activity in Southern California, at least among commercial banks. Wells Fargo pledged to continue Crocker’s attentiveness to that line of business, however in the years from 1990 to 1996, especially in the San Diego market, Wells Fargo divested itself of a great many of these types of business customers, even though it reported business lending of $1.3 billion at December 31, 1991, up from $1.0 billion at year-end 1990. Wells Fargo admits it focuses on small businesses with annual sales of up to $10 million in which the owner of the business is also the principal financial decision-maker. Credit products available to these businesses are “lines of credit, receivables and inventory financing, equipment loans and leases, real estate financing and SBA financing.” The Bank uses a focused product group that “utilizes automated credit decision methods . . . to approve or decline requests for credit.”

Yet, changes to Wells Fargo’s small business lending program is a prime example of the fact that the threat of competition from out-of-market institutions has arrived. As detailed in a recent press report, Wells Fargo pioneered a national small business loan program conducted through the mail. The program was initiated in 1992 in California, and has helped in-

522. See id.
525. See id.
528. Id. at 9 & 10.
529. Id.
crease Wells Fargo’s share of California’s small business loans from 1% to 20%. The program was expanded nationwide three years later, offering loans from $5,000 to $100,000 in all fifty states. The bank reportedly plans to make $25 billion in small business loans through the program over the next ten years. Recently, perhaps to address Wells Fargo’s past oversight of the female and African-American small business market, Wells Fargo launched a nationwide $41 billion African-American loan program in June 1998. “[Wells Fargo] then created a $1 billion latino loan program last year.”

In 1990, BankAmerica created the Bank of America Community Development Bank and the Community Development Division of Bank of America’s Federal Savings Bank as a way to combine its core products with community-based organizations and meet varying community credit needs. Between 1990 and August 1997, those entities developed a $1 billion portfolio of affordable housing and small business loans by partnering with federal and state public agencies such as the U.S. Small Business Administration, the U.S. Department of Housing and Urban Development, the U.S. Department of Agriculture, local agencies, and community-based non-profit organizations. “The bank established a $1 billion women’s loan program in 1995, which it expanded to $10 billion in 1996.”

In 1994, BankAmerica made $1.1 billion small business conventional and government assisted loans. The Advantage Business Credit program was introduced in 1992 in order to widen the availability of loans and credit lines under $100,000 to small business owners. That program nearly doubled in size in the first two years. During 1996, BankAmerica reports having made $409.6 million in “Special Small Business Programs,” which are loans under government-guaranteed and other programs for small businesses and for commercial improvement or development. The bank also reports $3,299.4 million in loans up to $750,000 each to conventional small business. BankAmerica considers itself “[t]he number one provider of SBA loans among banks in America and among the top providers of commercial and

531. See id.
532. See id.
533. See id.
535. Id.
537. Id.
539. See id.
541. See id.
industrial loans worldwide with more than $52 billion outstanding in 1997.\footnote{542}

In the San Diego area during 1995, BankAmerica extended a small business loan through its Minority- and Women-Owned Business Enterprise Program to The Bread Basket bakery which employs 12 people.\footnote{543} Admittedly, loans of this size are atypical of the large commercial banks, sometimes even under CRA programs. BankAmerica also joined with local government, through a partnership with San Diego City Councilman George Stevens and the San Diego Housing Commission, to complete the construction of a 54-unit affordable housing development that had been abandoned for eight years.\footnote{544}

Union Bank has also created minority- and women-owned vendor purchasing programs as well as minority- and women-owned business assistance programs. In 1994, Union Bank provided $24.7 million in small business loans, which contributed to the creation of 523 jobs.\footnote{545} Union Bank pledged $110 million in small business loans and lines of credit to nonprofit community organizations and small businesses.\footnote{546} The funds are administered through four California sites, including San Diego.\footnote{547}

It appears that the three major San Diego commercial banks have in recent years reaffirmed their commitment to San Diego’s small business market. The challenge for these banks, as they amalgamate, is to continue a commitment to the small business growth and the economic well-being in all the communities in which they currently operate, as well as every community into which they expand.

Often the Justice Department, in connection with a merger decision or an antitrust evaluation of a competitive geographic market, will restrict its competitive analysis to smaller geographic markets because it considers small business lending to be a local matter. Obviously tools like DOJ divestiture requirements, the elimination of legal barriers to geographic expansion of banking, and even the revolution of technology in the financial services industry are good for small businesses seeking competitive loan rates, and will help assure the commitments of major banks to meet those needs.
5. Have the Needs of the Depositors in San Diego Been Met During Amalgamation?

"'Banking' has existed for some 5,000 years." In that time, banking organizations have reinvented themselves repeatedly. The products available to the public have grown beyond comprehension. Both cash and checks have lost popularity to electronic transactions and credit exchanges. The stock of both banks and savings institutions are traded on various stock exchanges. Mutual funds and the borrowing public have, for the first time in years, the advantage of lower interest rates and a larger array of choices. All changes are due in large part to the competition that now exists between banking organizations.

Bank fees have markedly increased in California in recent years. Since 1990, Banks have introduced 150 new fees. A 1994 Federal Reserve Report, based on a survey of more than 1,000 banking organizations, found that "fees charged by out-of-state banks are significantly higher than those at in-state banks." The study also found that "services at banks were reduced in 1994. "Out-of-state banks usually are larger than in-state banks and may be concentrated in large cities where costs are higher."

A study by the U.S. Public Interest Research Group "compared fees of 271 banks in 25 states and the District of Columbia with a similar study of 23 states performed by the consumer group in 1993" and found that many checking and savings account fees rose in the past two years by 11 percent. In 1997, the same research group "surveyed 419 banks in 29 states and found that consumers paid on the average 15% more to maintain a regular checking account at a big bank. A June 1997 study by the Federal Reserve showed similar results. Stop payment orders at banks that operate in more than one state cost an average 30% more." There are now fees for calls to the bank which exceed the proscribed number and ATM access fees charged to non-customers are higher and more prevalent. But, big banks are more likely to receive governmental aid to avoid liquidity crises and pos-

548. Pat Dye, Jr., Case Note, Banking Law—Deposits and Collections—California Supreme Court Declares That NSF Charges May Be Held Unconscionable, 16 CUMB. L. REV. 393, 395 (1986). "The University Museum in Philadelphia has a clay promissory note of Babylon, circa 3000 B.C., which provides for repayment of principal and interest on a specified date. An Egyptian clay tablet, circa 2000 B.C., constituting an instrument payable to the bearer and promising repayment in produce of a loan in money, also has been found." Id. at 393 n.26 (citing Rufus J. Trimble, The Law Merchant and the Letter of Credit, 61 HARV. L. REV. 981, 982 (1948)).
550. Id.
551. Id.
552. Id.
554. See id.
sible failures.555

The bank-customer contract arises from special relationship features.556
"First, the customer ... is 'totally dependent' upon the bank's honesty and expertise. Second, ... [noneconomic motives, primarily convenience and security, encourage customers to open bank accounts.] Third, banks offer 'vital' services to the public."557 But the contract between the bank and customer is a standardized contract; like a contract of adhesion, it gives only two choices: adherence or rejection.558 Customers rate "convenience as the most important motivation for choosing a particular bank, [and] other important factors include recommendations, helpful personnel, and reputation."559

"The fear of large banks having too much power ... still exists in society today."560 But, regardless of what consumers think, there is no sign that bank mergers are slowing. In the first half of 1998, 277 bank mergers were announced worth $240 billion.561 Most customers, when their bank is bought, simply resolve themselves to live with the resulting merged institution. "Mark Caron was one of about 150,000 customers at Shawmut Bank who had a checking account that required a balance of $3,000 or $5,000 to avoid monthly fees. When Fleet Bank bought Shawmut in 1996, it promised to keep those accounts. But after about a year, Fleet eliminated them and shifted customers to one requiring a $10,000 balance. 'I wasn't pleased,' Caron says."

The past may have foretold the future. Looking back, perhaps "1987 [was] the 'crossroads' in the post-deregulation evolution of the [savings] industry ... [clearly] the optimism of 1985 and 1986 ha[d] come face-to-face with some disturbing realities as to whether there really is 'life after deregulation.'"562 While antitrust concerns remain a consideration in the path of amalgamation, gone now are the regulatory schemes that gave banks protective armor against outside competition. The competition in San Diego today comes not simply from national, regional, or local competitors, but from Pacific Rim banking organizations. For example, in 1996 "Bank of Tokyo's Union subsidiary [bought] the Mitsubishi-owned Bank of California."563 "The foreign banks in Southern California, the largest of which are Japanese

---

555. See Boro, supra note 240, at 466.
557. Id. at 1291-92.
558. See id. at 1291 n.88.
559. Id. at 1291 n.92.
560. See Tart, supra note 12, at 916.
564. Danielson, supra note 7, at 10.
owned, were somewhat protected from failure by deep-pocket parents, but they were not totally immune to problems and consolidation.\textsuperscript{565}

The new challenge in banking is technology, and how information processing will change the business of banking. "The exchange of information... is really what electronic financial commerce is all about. It is, therefore, inevitable that banks will join forces with technology and telecommunication providers."\textsuperscript{566}

Banks are already starting to develop virtual branches with no bricks and mortar. In a virtual branch, all bank products and services are being provided in an electronic format. But that's not all. A virtual branch can also offer other financial services, such as investment and insurance products. More importantly it can even offer services... for such things as financial market research, travel and entertainment arrangements and products, and online newsletters and magazines. The possibilities are countless. [Of course, in] a virtual branch all this [happens without regard to] geography and government borders, [which are] key factors in traditional antitrust analysis governing bank mergers and acquisitions.\textsuperscript{567}

Technology has transformed everything banks do... .

The goal: integrated, high-speed computer networks that sell everything from mutual funds and insurance policies to simple checking accounts, all aimed at consumers around the globe.

Such networks are "the fuel" of the bank consolidation drive, says Jim Dixon, president of technology and operations at NationsBank Corp., which recently announced a $60 billion merger with BankAmerica Corp. Customers, he says, want to do their banking anytime of the day and by using whatever "appliance" they choose, be it a phone, home computer, automatic teller machine, or other device... . Experts at IBM are now being called in as soon as a merger is finalized.\textsuperscript{568}

Consider the ongoing evolution of electronic banking and commerce:

- Nearly 1,000 banks have created or are in the process of creating Internet Websites to market their products and services. Some 94 insurance companies, and 40 securities firms also have done so. About 1.5 million securities accounts are now on the Web.
- Many banks have initiated home banking programs, offering full-scale services and 150 banks offer moderate scale programs.
- About 2.1 million households are engaged in home banking. Some 40 million customers are using online services such as America Online.\textsuperscript{569}

\textsuperscript{565} Id.
\textsuperscript{566} Smith & Ryan, supra note 372, at *15.
\textsuperscript{567} Id.
\textsuperscript{568} Matt Murray & Raju Narisetti, Bank Mergers' Major Engine is Technology, WALL ST. J., Apr. 23, 1998, at B1, B9.
\textsuperscript{569} Smith & Ryan, supra note 372, at *19-20; see also Murray & Narisetti, supra note 568, at B9 ("On-line banking is another way banks hope to keep customers happy and save
Yes, the way banking services are delivered will constantly change over the next millennium, but the needs of bank customers remain essentially the same as they were when the first savings bank was created in Boston in 1816. At the center of all this remains the customer, the depositor, without whom the growth of this industry would be largely irrelevant. These depositors continue to need banks to encourage savings, facilitate home ownership, and supply credit, and “for all the breakthroughs, many of the advances that technology can bring are more promise than reality. Many customers still prefer doing business at their local branch. PC banking has yet to take off as optimists have been projecting for years. And integrating computer systems will be one of the biggest headaches for newly merged banks.”

VIII. The Current San Diego Financial Market

San Diego County is California’s second highest populated area with almost 2.9 million residents, the country’s fifth largest population. In 1986, San Diego ranked among the top forty economies in the world. Today it remains one of the top economies in the world.

The discrepancy in asset size and services alone of the ten banking organizations that remain in San Diego is astounding. Of the major commercial banking organizations, BankAmerica with $263,527 million in total assets is at the top of the market. Wells Fargo Bank follows with $97.5 billion, and Grossmont Bank with $628 million in assets is the leader of the small commercial organizations. There are no savings institutions which remain a factor in the local banking equation, but there has been a tremendous development in the size and services of the local credit unions, which now number 19 and have $4,350,200 million in total assets, 1,707 employees, and 108 branch offices collectively.

Corporate restructures, mergers and acquisitions, the nationalization of banking, layoffs, and cost containment efforts have reduced the time commitments banking executives in the past pledged to community involvement. In some cases, the monetary support financial institutions gave to the community has also been reduced. In past years, the major banking organizations

money. It typically costs 90 cents to $2 every time a customer does a transaction with a bank teller. That falls to about 40 cents at an ATM, but costs around a nickel on the Internet.”

570. See Ernst, supra note 15, at 97.
572. The Dec. 31, 1998, forecast figure is 2,869,437 residents. Selected Economic Indicators, supra note 387, at 53.
doing business locally were headquartered in San Diego, now the largest banks are nonlocal. Some do not consider themselves corporate citizens of San Diego, except for CRA purposes.

1. Wells Fargo Bank

"Among commercial banks, [Wells Fargo was] the second largest holder of customer deposits in California" in 1996. Other than this, it is difficult to calculate a real meaningful measure of overall market share within the broadly defined financial services industry. "Ongoing consolidation has increased pressure on [Wells Fargo] from its most significant competitor in California, [BankAmerica, which was] the third largest bank holding company in the United States based on assets as of December 31, 1996. [F]ederal and state legislation adopted in recent years has increased competition by allowing banking organizations from other parts of the country to enter [Wells Fargo's] core geographic market." On January 20, 1998, Wells Fargo reported "net income of $298 million for the fourth quarter of 1997, compared with $123 million for the fourth quarter of 1996. [Fourth quarter] [p]er share earnings were $3.40, compared with $1.12 in the fourth quarter of 1996." For first quarter 1998, Wells Fargo announced net income of $315 million and net interest income of $1.13 billion, as compared to $1.21 billion in the first quarter of 1997. The decrease from a year ago was attributed to a decline in earning assets. Wells Fargo total assets at the end of first quarter 1998 decreased to $94,820 million from $101,863 million at the end of first quarter 1997.

Wells Fargo Bank is headquartered in San Francisco, California. On December 31, 1996, Wells Fargo Bank had 1,947 retail outlets, comprised of 1,274 traditional bank branches, 298 supermarket branches, operated 2,672 ATMs and 375 banking centers in tenth western states, located in San Diego County. The bank reports having 1,350 employees in San Diego. Outside of San Francisco, Los Angeles and San Diego have the largest number of Wells Fargo branch offices. During 1997, the bank announced its

579. Id.
582. See id.
583. See id. at 3.
586. See id.
587. See generally WELLS FARGO & Co., 1991 10-K REPORT 14 (1992); see also WELLS
plan to open 450 new retail outlets in Safeway stores in the Western United States. By January 1998, Wells Fargo operated 897 in-store branch offices. Wells Fargo reported assets of $50,316 million on December 31, 1995, and $108,888 million in assets at December 31, 1996; it had generated net income of $1,032 million and $1,071 million in 1995 and 1996 respectively. This tremendous growth in a one year period is directly attributed to the First Interstate acquisition completed April 1, 1996. This kind of growth has never been achieved as quickly, other than through amalgamation. As of December 31, 1997, Wells Fargo had assets of $97.5 billion, deposits of $72.2 billion, 33,100 full time employees, and was the 10th largest bank holding company in the country.

2. BankAmerica, National Trust & Savings Association

As the largest West Coast bank and the largest bank in California, BankAmerica reported net income of $812 million and profits from fees and other noninterest earnings of $1.63 billion in the fourth quarter of 1997. At year-end 1997, the bank had representative offices in 38 countries, maintaining 973 branches in California. The bank is a wholly owned subsidiary of BankAmerica Corporation. BankAmerica Corporation, headquartered in San Francisco, is the one of the largest bank holding companies in the United States. BankAmerica Corporation operates several other chartered financial institution subsidiaries in California, Nevada, Oregon, Alaska, Washington, Arizona, Texas, Illinois, Idaho, and Hawaii.

Even though BankAmerica is supervised by several different federal and state regulatory agencies, the Federal Reserve Board has primary responsibility for the supervision of the holding company, BankAmerica Corporation. As of December 31, 1997, the bank had total assets of $260.2 billion, total deposits of $172 billion, with total loans of $167 billion. The bank's primary business is retail and wholesale banking. BankAmerica has over 90,000 employees in 38 countries around the world, and 2,500 in San Di-
ego County. The BankAmerica’s reputation is that of an extremely well managed banking organization, highly profitable, and protective of shareholder investment. For example, “per share earnings rose more than net income because BankAmerica bought back 31.7 million shares of its common stock during the year.” The buyback apparently incited the increase to per-share earnings. “In the face of falling currency, stock and bond markets in Asia, BankAmerica retrenched, cutting its outstanding assets in the region by 13% to $14.1 billion during the period while earmarking about $400 million of its existing loan loss reserves to cover its Asian exposure.” As a result of its aggressive actions, the Bank’s depositors and customers are also well protected. BankAmerica’s major business activities are commercial, corporate lending and business services, and real estate lending.

3. Union Bank of California

The three major commercial banks doing business in San Diego are all headquartered in San Francisco, but Union Bank has openly declared its principal San Diego location to be its regional headquarters. UnionBanCal Corporation, a holding company which owns Union Bank, also headquartered in San Francisco, is itself owned by The Bank of Tokyo-Mitsubishi, Ltd., the world’s largest bank, with assets of $750 billion and a branch network of over 450 offices worldwide. Union Bank is the third largest bank in California, reporting assets of $29 billion at December 31, 1996, 243 branches on the West Coast, 238 in California, 65 in San Diego County, three in Washington, two in Oregon, facilities in Texas and New York, and 17 overseas branch and business offices. The bank considers itself to rank among the top 25 banks in the United States.

The bank is a full-service commercial bank providing a broad mix of financial services, including business lending, commercial and corporate lending, trust and investment management services, real estate-oriented services, and private banking. Union is in a head-to-head competition with Wells Fargo and BankAmerica for commercial bank market share. While their business focus (consumer and small and middle-market business

602. Id.
605. See id. at 1.
606. See id.
607. See id.
608. See id.
banking services) is slightly different than either of their competitors, Union Bank’s strategy is to entrench itself more visibly in the communities in which it conducts business. Its CRA activities, conducted through seventeen different programs, appear to be conducted more vigorously than the other two major San Diego commercial banks. In fact, CRA matters were emphasized independently in the three banking organizations that made up Union Bank prior to the April 1996 rebirth of the bank. Union Bank continued the community-based approach the three separate banks projected before the organizations were combined. This approach has given Union Bank a particular character and authority in both the San Diego business community and the community at large.

4. Great Western Bank/Washington Mutual, Inc.

There is immense speculation among industry analysts on the future of Southern California savings institutions. What is not intangible however, is the role Great Western Bank (now Washington Mutual as of July 1, 1997) will play in this scenario. Great Western’s financial strength, and position in the market, made a perfect springboard for entry into the southern California market by a national bank or one of the large regional savings institutions, and has long drawn the attention of financial institutions vying to do business in the lucrative San Diego market. Its acquisition was quite an accomplishment for Washington Mutual. Typically, the Southern California savings institutions are mortgage banks. They do not have assets compatible with commercial banks and are not well positioned to do the business of commercial banks. However, during 1996, Great Western reported non-interest-bearing checking accounts in excess of 5% of assets to liabilities and demonstrated it was well diversified in commercial real estate, consumer loans, securities, and mortgages.

In the fall of 1996, San Diego waited to see how the potential rival bidders for Great Western Financial Corporation, the target of a $6.34 billion hostile bid from H. F. Ahmanson would fair. The financial analyst community surmised that Wells Fargo & Company and BankAmerica Corporation, both growth-hungry California-based market contenders, would not be in the mix because of antitrust concerns. NationsBank, Golden West Corporation, Washington Mutual Inc., and First Nationwide Holding Inc. were all possible suitors for Great Western. Great Western did business mostly in California, with 46 branches in San Diego, and had at that time approximately $43

609. Southern California First National Bank, California First Bank, The Bank of California, and Union Bank were combined in 1975, 1988, and 1996 through mergers and acquisitions by The Mitsubishi Bank and The Bank of Tokyo, Ltd., to form what is now Union Bank of California.


billion in assets. Washington Mutual planned to consolidate only 2 branches by May 1998, leaving 44 Washington Mutual branches intact in San Diego. Analysts predicted that if the hostile bid by Ahmanson was unsuccessful, Washington Mutual was the best poised of the rival bidders.

Washington Mutual had a record of proving its ability to convert savings institutions from deposit-centered institutions to successful retail banking operations. As early as 1987, Washington Mutual had begun to move into the acquisition and merger scenario with their initial acquisition of three branches of Shoreline Savings Bank. Even though Washington Mutual, based in Seattle, just completed its latest of 22 acquisitions in the last ten years with the acquisition of American Savings during the summer of 1996, it had a record of consistent earnings growth. In late 1996, its stock traded in higher multiples as related to earning and book value than any other rival bidders. As a result of its experience acquiring other banking organizations, the bank anticipated (and realized) the systems integration of Great Western to be completed by the end of the second quarter of 1998. By year-end 1997, Washington Mutual had assets of $96,981 million, deposits of $50,986 million, and net interest income of $2,656 million.

Washington Mutual is well capitalized after the Great Western merger, reporting for December 31, 1997, stockholders’ equity of $5.31 billion, compared with $4.99 billion at year-end 1996. At the end of 1997, the ratio of capital to total assets was 5.47% compared with 5.71% a year earlier. The company had 19,880 employees as of year-end 1997.

The bank is regulated as a S&L holding company by the OTS, the Director of the Department of Financial Institutions of the State of Washington, the FDIC as a state-chartered bank, FDICIA requirements, and the Federal Reserve Board. The bank’s deposit accounts are insured by the FDIC through both the BIF and SAIF.

613. See id.
615. See id.
619. See id. at 1.
620. See id.
621. See id.
623. See id. at 14-20.
Washington Mutual faces significant competition in attracting and retaining deposits and making loans in all of its market areas. Its most direct competition for deposits has historically come from savings institutions, credit unions and commercial banks doing business in its primary market areas of California, Washington, Oregon, Florida and Utah. As with all banking organizations, however, Washington Mutual has also experienced competition from nonbanking sources, including mutual funds, corporate and governmental debt securities and other investment alternatives. Washington Mutual’s competition for loans comes principally from savings institutions, commercial banks, mortgage companies, credit unions, insurance companies and other institutional lenders. Many of these competitors have more significant financial resources, larger market shares and greater name recognition than Washington Mutual. The activities of such competitors may make it difficult for Washington Mutual to achieve its financial goals. In addition to the normal competitive factors described above, Washington Mutual management at the holding company level has limited operating experience in California and Florida, each of which has a much larger population with more large financial institution competitors than the states in which Washington Mutual has historically operated. Accordingly, there can be no assurance that Washington Mutual’s consumer banking strategy will prove successful in the California and Florida markets.

Although consolidation has decreased the number of institutions competing in Washington Mutual’s market, both savings and commercial banks have reemphasized their focus on the consumer, making competition for retail deposits and loans extremely fierce. While the increased competitive pressures make the banking environment more difficult, the Company remains a strong market force. For 1997 (through October), Washington Mutual’s originations of single family residential loans ranked first in both Washington, Oregon and California.

Now serving over four million customers in 10 states, there is every expectation Washington Mutual will retain its market share of Great Western San Diego customers.

5. The Locally Based Financial Institutions—Grossmont Bank, Bank of Commerce, Scripps Bank, Peninsula Bank, and North County Bank

These five local banking organizations are currently extremely likely takeover targets for regional or national financial institutions looking to increase their presence in the San Diego banking market.

a. San Diego National Bank

During 1997, San Diego National, a commercial organization, headquartered in downtown San Diego, emerged as one of the local small bank leaders. In July 1997, the Bank received approval from the Comptroller of

625. Id. at 20.
the Currency to purchase ten Regency Savings Bank branches in San Diego County. Even though both Regency Savings and San Diego National are owned by FBOP, a financial holding company based in Illinois, the acquisition gave San Diego National assets of about $930 million and 12 branch offices in the county. This deal made the Bank the largest locally based financial institution of either the commercial or savings banking organizations.

At the time of the acquisition, San Diego National immediately announced it would place a new emphasis on consumer banking products and extend its lending limit for business customers from $2 million to $25 million. As of December 31, 1997, San Diego National reported $201 million in assets, and $171 million in deposits. The majority of its business (60%) is commercial loans, including loans to business and agriculture. Thirty-five percent of its business is real estate loans.

[The Chief Executive Officer very publicly] emphasized [the bank's] local ties and the human touch in describing the mission of the expanded . . . Bank, [saying] personalized customer service and participation in the civic and arts communities as well as direct interest and flexibility to meet the financial needs of San Diego's business sector has been lost through mega-national bank mergers . . . [O]ur goal is to fill this void.

He also insisted that no layoffs were expected, rather the bank actually anticipated some hiring. Prior to the Regency purchase, the bank had 108 employees. "San Diego National Bank reported year-to-date net earnings at the end of the [third- quarter 1998] of $11.04 million, compared to $1.8 million for the same period in 1997. The privately owned bank had net third-quarter earnings of $3.01 million, compared to $1.31 million for the third quarter of 1997."

It is institutions like San Diego National and Grossmont Bank that will attempt to transform the void left in the San Diego financial market, by the disappearance of Great American, Imperial Savings, Home Federal, and San


630. See Berliner, supra note 628, at C2.


632. See id.

633. See id.


635. See Berliner, supra note 628, at C2.


b. Grossmont Bank

Grossmont Bank is considered by industry analysts to be one of the highest performing banks among the largest publicly traded banking companies in the nation. On December 31, 1986, Grossmont had nine branches, 236 employees, $265 million in assets, and deposits of $236 million. Prior to the Zions purchase in 1996, Grossmont earned $101.7 million in net income, and had $7.7 billion in assets. As of Dec 31, 1996, the bank reported total assets of $628 million and net income of $6.5 million. As of December 31, 1997, Grossmont had earned an $11.4 million net income, reported total assets of $858 million, and deposits of $776 million. Organized in 1972 in San Diego County, from its humble beginnings Grossmont has grown to 13 local branches, with 281 employees.

c. Bank of Commerce

Bank of Commerce became the largest independent San Diego based commercial bank when Zions completed the Grossmont acquisition in 1997. Founded in 1975, by 1987 the Bank reported $92 million in assets, $85 million in deposits, four local branches, and 95 employees. Today Bank of

639. On July 9, 1997, Grossmont Bank (which had been the largest locally-based bank prior to the San Diego National deal) accepted an out-of-state buyout offer worth $173 million in stock from Zions Bancorp, a Utah holding company with banks in four states. Zions appears to prefer, and is recognized for its expertise in, acquiring banking organizations in select markets like San Diego and leaving the management of the acquired institution in the hands of the local managers who are familiar with the corresponding local communities. Zions currently operates small community-oriented banking organizations in Utah, Arizona, Nevada, and Colorado, and in 1997 entered into a deal to purchase 31 branch offices from Wells Fargo in Idaho, Utah, Arizona and Nevada. See generally Michael Kinsman, Grossmont Bank Accepts Out-of-State Buyout Offer, SAN DIEGO UNION TRIBUNE, July 12, 1997, at A1.
641. See id.
642. See Largest Banks, supra note 629, at 18.
Commerce has grown to assets of $375 million, deposits of $345 million, five local branches, and 142 employees. Its business is almost exclusively commercial lending, including business and agricultural loans.


d. Scripps Bank

Scripps Bank had not been a significant force in the San Diego banking market, having only three branch offices until 1997 when the bank expanded to seven branch offices and began to concentrate on the trust business. In 1987, Scripps reported $59.3 million in assets and $54.6 million deposits. At that time there was one branch and 31 employees. As of December 31, 1996, Scripps had $301 million in assets, $271 million deposits, and 170 employees. About one-half of the banks lending is commercial loans, the other half in real estate. By December 31, 1997, Scripps reported 189 employees, 7 branches, a CRA rating of 0.96%, a net income of $3.2 million,

647. See id.
649. See id.
650. See Largest Banks, supra note 629, at 18.
652. See id.
656. See id.
658. See id.
total assets of $387 million, and $353 million in deposits.\textsuperscript{659}

e. Peninsula Bank

Peninsula Bank was founded in 1975 in San Diego County.\textsuperscript{660} By year-end 1986, Peninsula Bank had assets of $141 million, net loans of $78 million and deposits of $132 million.\textsuperscript{661} It maintained only three branch offices in San Diego and 120 employees.\textsuperscript{662} As of December 31, 1996, the Bank reported 216 employees, $343 million in assets, $318 million in deposits, and a CRA rating of outstanding.\textsuperscript{663} The majority (63\%) of its business is making real estate loans.\textsuperscript{664} Peninsula Bank is now the fourth largest commercial bank based in San Diego.\textsuperscript{665} It continues to report a CRA rating of 0.95\%.\textsuperscript{666} The bank has grown to 10 branch offices, 240 employees, reports $417 million in total assets, $389 million in deposits, and a net income for December 31, 1997, of $3.6 million.\textsuperscript{667} "Peninsula Bank [reported] record operating results for the nine-month period ended [September 30, 1998.] Net profits were up 46.4 percent for the third quarter, while net profit for the nine months ended [September 30, 1998.] were up 37.8 percent . . . Peninsula Bank was one of the top dollar gainers on the San Diego Stock Exchange on [October 20, 1998]."\textsuperscript{668}

The locally based banking organizations are tiny establishments compared to the three conglomerates in San Diego. This is the choice San Diego depositors have, either pay to speak to a customer service representative at their big bank after their pre-determined number of allotted calls each month, or call or walk up to their small local bank for personal attention. This is not too difficult of a choice for most depositors.

At the same time, it appears "that the acquisitions of Security Pacific, Crocker and First Interstate by BankAmerica and Wells Fargo have foreclosed other meaningful large bank competition . . ."\textsuperscript{669} Deposits, after all, are supposedly one measure of a financial institution's competitive capacity; Wells Fargo and BankAmerica lead California banking organizations in deposits.\textsuperscript{670}

\textsuperscript{659. See Largest Banks, supra note 629, at 18.}
\textsuperscript{660. See Top 25 Area Banking Companies, SAN DIEGO BUS. J. BOOK OF LISTS, Dec. 1987, at 29.}
\textsuperscript{661. See id.}
\textsuperscript{662. See id.}
\textsuperscript{663. See Largest Area Commercial Banks, SAN DIEGO BUS. J.—THE LISTS, Dec. 1998, at 52.}
\textsuperscript{664. See id.}
\textsuperscript{665. See Largest Banks, supra note 629, at 18.}
\textsuperscript{666. See id.}
\textsuperscript{667. See id.}
\textsuperscript{668. Grupe, supra note 651, at 6.}
\textsuperscript{669. Danielson, supra note 7, at 8.}
\textsuperscript{670. See Appendix A, infra.}
In California, however, banks are only part of the banking story because the state is home to most of the nation’s largest savings institutions. Ahmanson & Company’s Home Savings subsidiary and Great Western [now Washington Mutual] had combined deposits of more than $20 billion, and a resuscitated American Savings, Golden West, CalFed, GlenFed, Coast Savings, and First Nationwide also are important players and are larger than all but three banks in the state.

...[T]he large S&Ls are rapidly becoming all that is left of savings institutions that once held almost 50 percent of California’s deposits.671

In 1986 there were 16 thrifts doing business in San Diego.672 They ranged from Morris Plan Thrift and Loan with $383 million in assets to the San Diego based Mission Thrift and Loan with $12 million in assets.673 “Eleven large thrifts hold about 29 percent of California’s deposits, which is up from the 24 percent they held in 1990. The rest have done less than 6 percent, or less than one-third of what they had five years ago.”674

It appears that savings institutions have finally stabilized. As a result, it is no longer considered necessary to have a separate government agency to supervise the bailout of the savings and loan industry; consequently, in December 1995 the Resolution Trust Corporation closed down, and the FDIC assumed responsibility for the functions of the RTC.675

As the economy improves, the problems of many banks and savings institutions are dissolving. Some perception of reluctance to invest remained in California banking, at least until the announcement April 13, 1998, of the pending merger between BankAmerica and NationsBank and the November 1998 announcement of the Wells Fargo/Norwest merger. California banking is now on the threshold of yet another period of extended growth. Which institutions will participate is an open question, but whether amalgamation will continue as the preferred manner of growth seems certain.

What is not an open question is who commands the top position in California banking. BankAmerica has long been the leading California bank, its presence is a vital part of the city of San Diego. [The dark days of the mid-1980s, when BankAmerica’s survival was a concern and Security Pacific, Wells Fargo, and First Interstate were challenging its supremacy, are long past. Wells Fargo is now the most formidable competitor and other than Union Bank, all its other major competitors are gone.]676

“Today California’s banking can be summarized as two very large banks competing statewide against a myriad of local banks that are a fraction

671. Danielson, supra note 7, at 7-8.
673. See id.
674. Danielson, supra note 7, at 8.
676. Danielson, supra note 7, at 6.
their size, a few Japanese-owned banks and some very large thrifts, the majority of which are in the Los Angeles area.\textsuperscript{677}

IX. CONCLUSION AND RECOMMENDATIONS

"[T]he only certainty about the future is that BankAmerica and Wells Fargo will be the market leaders,"\textsuperscript{678} especially in San Diego. But, Union Bank is the third largest commercial bank in California, reporting $31 billion in assets and $23 billion in deposits.\textsuperscript{679}

In its July 1993 report to the President and the Congress of the United States, the National Commission on Financial Institution Reform, Recovery and Enforcement made several highly respected recommendations in the areas of regulation and supervision, abuses and fraud, and as guardians of the public interest. The Commission proposed "all federally insured depository institutions should be subject to federal rules, regulations, and examination which would supercede state rules, regulations and examinations upon a finding that state-sanctioned activities threaten the safety and soundness of the insurance fund."\textsuperscript{680}

The FDIC would encourage experimentation in the states concerning new powers and other issues, provided they are consistent with safety and soundness.\textsuperscript{681} Citing the "poor record" of S&L regulation and the elimination of the distinction between banks and thrifts, the Commission further proposed "the FDIC be made the sole federal insurer of depository institutions and the sole federal charterer and regulator of insured depositories."\textsuperscript{682} The FDIC would remain an independent agency but would be required to consult regularly with the Federal Reserve and make available to it, on a timely basis, all pertinent information concerning the condition of insured depository institutions.\textsuperscript{683} Certainly implementation of such a reform would eliminate the inconsistencies between California financial corporation regulations and the federal banking regulations, which led to some of the earlier loopholes San Diego based savings institutions utilized to broaden their products and services repertoire and amalgamation activities. To date, such basic and practical reforms suggested by this 1993 report have still not been embraced.

With regard to abuse and fraud, the Commission first acknowledged that "savings institutions were tempting vehicles for abuses and fraud, and there were greatly increased risks of loss from those sources."\textsuperscript{684}

The Commission acknowledged, "insured deposits combined with non-
existent net worth requirements allowed massive growth to keep ponzi-schemes going and to maintain access to additional sums to prevent collapse. Cash could be easily withdrawn from an institution either directly through salaries, bonuses, perks, and dividends, or indirectly through nominee loans, kickbacks, and other devices. Moreover savings institutions were cheap to acquire. It was easy to get approval to control the entity and easy to dominate it. The regulatory laxity introduced as a part of forbearance provided the ideal fraud environment. It allowed the fraudulent to report financial strength and disguise losses while savings institutions were being looted. It required no financial risk from those engaged in the fraud, and offered little chance of the fraud being discovered, proved and punished. Because of the application of FDICIA, BHCA and increased examination and regulation by the FDIC, OTS, and state supervision, this is no longer true in 1998.

In fact, in past years FSLIC and the FHLBB regularly required healthy savings institutions to take over and manage problem financial institutions as a quid pro quo for regulatory approval of such an institution's request to complete a highly sought after merger or acquisition. FSLIC efforts to conserve cash by arranging takeovers of insolvent savings institutions, rather than closing them and paying off depositors, also contributed to the problems. Given the ability of the acquirers to contribute real estate and/or borrow the minor capital infusion, it cost almost nothing, or less than nothing (as where the S&L paid the acquirer cash for the excess value of the real estate contributed) to buy a S&L. But the problems in the S&L industry were not just deregulation, poor capitalization or deposit insurance.

During San Diego-based Great American First Savings Bank's March 1986 acquisition of Home Federal Savings and Loan Association of Tucson, Arizona, in addition to paying "cash in the amount of $103.5 million to acquire Home Federal," the FHLBB required and FSLIC assisted Great American to acquire two insolvent institutions operating under FSLIC-imposed conservatorships: Hacienda Federal Savings and Loan Association, Oxnard, California ("Hacienda Federal") and First Federal Savings and Loan Association of Redding, Redding, California ("First Federal"). The total assets of Hacienda Federal and First Federal at December 31, 1985 were $74.6 million and each of them operated a single office.

... [These acquisitions were treated as part of the same transaction in which Great American acquired Home Federal of Tucson. FSLIC first] placed Hacienda Federal into receivership and liquidated it, selling substantially all of its assets and liabilities to First Federal. [Pursuant to an Assistance Agreement among FSLIC, Great American and First Federal,] FSLIC agreed to provide certain financial assistance to Great American.

---

685. Id.
686. Id. at 70.
687. Id.
Under the Assistance Agreement, [FSLIC agreed to] contribute to Great American the amount of the negative net worth of Hacienda and First Federal over $24 million . . . . In addition, losses or profits realized upon the disposition of certain assets of Hacienda Federal and First Federal at the acquisition date . . . [would be] shared equally by Great American and FSLIC. [Finally, FSLIC] agreed to indemnify Great American against certain losses or claims that [arose] out of its acquisition of Hacienda and First Federal. 688

What banking organization interested in amalgamation would not be willing to acquire troubled institutions pursuant to such an agreement?

Amalgamation in such an environment only increases the possibilities and depth of such abuses to occur. Certainly federal and state political affiliations between both owner-controlled and manager-controlled banks and savings institutions had a role in the latitude certain financial institutions were given in regulatory compliance matters and merger and acquisitions deals. The Bank Board still promotes some quid pro quo arrangements in exchange for regulatory approval, but today the anti-competitive effects of a merger managed through divestiture plans are more of a regulatory concern.

Given such acknowledgments, the Commission recommended the Federal Reserve Board, FDIC, SEC, Treasury and Justice departments, and the legal and accounting professions take proactive roles in formulating specialized rules of professional responsibility for attorneys and accountants representing institutions receiving federal insurance or guarantees to try to keep criminals away from insured institutions, and aggressively prosecute wrongdoers, for the deterrent effect. 689 It appears however, that the most convincing deterrent has been the shareholder derivative suits which began in response to the amalgamation of the 1980s and show no sign of retreating today.

The Commission advocated creating anti-fraud units that would include attorneys, investigators, and accountants within each federal agency to be responsible for regulating financial institutions and refer criminal matters to individual U.S. Attorney’s Offices or other such agencies. 690 The Commission’s idea was to make each federal agency responsible for regulating institutions which receive federal insurance or guarantees under its jurisdiction accountable, even to the extent of “appointing an inspector general (‘business practices officer’) periodically to review and report upon the practices of the institution. [Such an] inspector general would be appointed for a fixed term (e.g., five years) subject to the approval of the federal regulatory authority. [This] inspector general could not be removed by the institution—except upon approval of the regulatory authority.” 691 Still there has been no attempt by the regulatory banking agencies to establish these “task forces” of

689. See ORIGINS & CAUSES, supra note 42, at 71.
690. See id.
691. Id.
sorts to more closely scrutinize fraud within financial institutions.

Finally, the Commission made certain recommendations pertaining to the federal government’s role as guardians of the public interest with regard to the financial services industry. The problem, according to the Commission, was conflict of interest and improper separation of powers. The Bank Board’s role was “protecting taxpayers by assuring the safety and soundness of the S&L industry . . . . [But h]istorically the Bank Board served more as the promoter of the S&L industry than as its stern regulator.”692 When economic anomalies occurred in the financial market, FHLBB was ill-equipped to deal with the long term ramifications and responded by “promoting long term growth [in areas other than housing finance, and creating] strong incentives for [savings institutions] to pursue risky and abusive ventures.”693 The Executive Branch was focused on reducing government, cutting taxes and increasing national defense, and election year politics, and Congress delayed recapitalization of the FSLIC, limited the statutory authority to deal with mounting problems, and took heed to the assertions of industry lobbyists and even regulators who insisted the problems were under control, failing to recognize news media reports, revelations, and criticisms.694 The National Commission on Financial Institution Reform, Recovery an Enforcement considered the news media “key guardians of the public interest,”695 and charged the media with “failing to sound an alert with respect to the unfolding S&L crisis.”696

As this report suggests, the answer is to improve the performance of the guardians, and “[make] the burden [of these guardians more] . . . manageable by assuring that the perverse incentives—economic, political and bureaucratic—that created the S&L debacle are eliminated.”697 But for banking organizations in 1998, some of these particular inspirations remain. The Commission’s answer is to have “Congress delegate to the Federal Reserve Board authority to appoint a nonpartisan oversight board,” an objective group without rule-making authority, to oversee and comment on issues relating to federal deposit insurance and regulation.698 This group would consist of “members . . . [with] expertise in accounting, legal and economic issues,”699 its charge being to “publish an annual report, testify at oversight hearings . . . issue press statements on matters concerning deposit insurance and regulation . . . [and] evaluate proposed new statutes, rules, regulations and examination procedures that appear too lax or that industry representa-

692. Id. at 72.
693. Id.
694. See id. at 73-74.
695. Id. at 74.
696. Id.
697. Id. at 75.
698. Id.
699. Id.
tives indicate represent an undue burden." The idea was for this oversight board to "evaluate federal deposit insurance programs . . . [with] particular attention to the presence or absence of moral hazard . . . [and] evaluate both estimates of exposure to loss by these federal insurance programs." The Commission advocated full "authority, budget, and qualified staff . . . [for this board, in order to] build the board's standing in the public arena . . . generate confidence and promote political action on long-term problems which had been ignored" in the past.

The Commission admits "[c]ongressional oversight was inadequate and ineffective during the collapse of the S&L industry," and finds not only that "congressional committees need better access to information without relying only on regulators" but that the view of these committees could also be "enhanced by the expertise and perspectives available by establishing visiting scholar programs for academic experts."

This Commission concluded that "a more vigilant news media with reporters better trained in economic and financial affairs could contribute much to keeping pressure on Congress and the Executive Branch to prevent future debacles from occurring." The problem is that the news media should not be charged with playing a role in discovering flaws in a system that is the Federal Reserve Board's and the other regulatory banking agencies' responsibility. True, the news media is, of course, the ultimate guardian of the public interest; but for regulators to trust even financially astute reporters with the responsibility of evaluating federal deposit insurance programs and regulatory actions is not appropriate.

Big savings institutions with a high concentration in the San Diego market have a rosy future there. Housing development in San Diego is experiencing a strong recovery which means mortgage lending is again in as much demand as commercial banking services. Although savings institutions have always been primary receptacles of insured deposits, it does not appear they will continue to be as much of a factor in the San Diego market as commercial banks.

The problem is that so few savings institutions remain in the San Diego market, and credit unions are ill equipped to service large numbers of customers on a large scale. Certainly credit unions have been and will increasingly have a competitive impact on the locally based banking organizations and the markets they service. In San Diego, credit unions account for an increased percentage of bank and savings institution deposits, and aggressively compete with traditional financial institutions in terms of products and services. On December 31, 1996, there were over twenty-five large credit unions.

700. Id.
701. Id.
702. Id. at 75-76.
703. Id.
704. Id.
doing business in San Diego.\textsuperscript{705} Membership in credit unions is no longer restrictive, now opening up to nearly every individual or business in the market. But the tide of amalgamation will not slow. Now that the industry has moved away from government regulation toward a market in which each banking organization is vulnerable only to market conditions and competition, there is no reason to turn back to the methodical days of banking. In creating the future, banking organizations will have plenty of opportunity for innovation and adaptation. Certainly these conglomerates, products of amalgamation, can keep the needs of customers and communities as a focus. This should be a matter for the examination of the Subcommittee on Anti-Trust, Business Rights and Competition of the Senate Judiciary Committee and the House Banking Committee during the scheduled hearings on mergers in April 1998.

Banking institutions fulfill vital roles in the United States’ economy. The public relies on them to fulfill essential depository and intermediary functions. In their depository capacity, banks act as fiduciaries in the safekeeping and safe handling of public savings and fiduciary accounts. In their intermediary capacity, banks serve as reinvestment vehicles, channeling funds to meet consumer and business credit needs. In addition, banking institutions serve as payments intermediaries, providing liquidity to both consumer and business customers. These banking functions create a public interest in the soundness of the banking system that arises from a government’s obligation to protect customer expectations of safekeeping and from a government’s desire to promote a viable and efficient economic system.\textsuperscript{706}

The requirements to maintain an account at larger banks become more stringent with each super-regional mega-merger. Yet, there are fewer services available, except for those depositors who can maintain accounts of $10,000 or more.\textsuperscript{707} In addition, large multistate banks tend to use monopoly power to charge higher fees.\textsuperscript{708}

Over the last decade, the winners in financial services have been the category killers. These include specialized companies like MBNA in credit cards, Countrywide Credit in mortgages and GEICO in auto insurance. These organizations used technology to lower their costs and they improved their marketing, thereby taking customers from their more traditional counterparts in the staid banking world . . . . The financial services companies that are pairing up in the latest round of mergers want to trump the category killers by offering financial consumers the convenience of the shopping mall. The trouble is that there is little evidence that big companies can sell myriad financial products to all their customers . . . . "Typically families in the top half of the income structure deal with between

\textsuperscript{708} See id.
five and ten financial firms," [according to] Scott Cook, chairman of Intuit, Inc., the maker of Quicken software.

As it is with much in life, perhaps as it has always been in banking, increasingly those with minimum accounts of $10,000 to $15,000 on deposit get the best bank services.

Canadian Imperial Bank of Commerce is testing an ATM that can dish out stock certificates, money orders, insurance forms and savings bonds. The machine, developed by Compaq Computer Corp.’s Tandem unit and NCR, can tap into a data base to provide customized service, such as remembering that Mr. Smith likes to make withdrawals in $50 dollar bills. The new software is helping banks prioritize customers. These days ‘relationship managers’ know exactly which big customers are profitable and which aren’t. The software, which links to the bank’s databases, allows Chase Manhattan Bank executives to negotiate higher fees on certain services or put in a low bid for another piece of the customers business because the customer is generating higher fees in other areas. The same software prioritizes incoming customer phone calls, putting more-profitable customers ahead of others.  

Another problem is that when newly merged banks consolidate operations, the branch offices they close tend to be concentrated more heavily in poorer neighborhoods. “The number of banks and savings institutions have declined as a result of deregulation, acquisitions and failures, to 10,922 in 1997 from 18,193 in 1981. But at the same time, the number of bank branches has remained relatively stable, around 83,000, meaning consolidation has not had an adverse effect on convenience.”

“From a community bank perspective, southern California is the land of opportunity . . . . [It is a] market with $250 billion deposits, only two large banks to compete against, a reduced savings institution presence, the largest foreign banks in the process of merging, and no [outsiders. It] is a local bank’s dream.” The small locals, Grossmont Bank, San Diego National Bank, Peninsula Bank, Scripps Bank, and First National, will be called upon by depositors to fill the vacancies left by the recent departures of First Interstate, San Diego Trust, and Security Pacific. The small locally based, community-oriented banking organizations are here to stay. Their strength will always be depositor relationships, the provision of personalized customer service.

Amalgamation has made it unlikely that banking organizations in a city like San Diego, or even nationally, be sensitive to the needs of the commu-
nities in which they operate, or ultimately to the depositors they seek. The question then becomes whether service to community or customers remains any part of the goal of capitalist banking organizations. "There are few, if any, institutions that so profoundly affect the public interest, but are so universally misunderstood, as banks. In the FDIC's view, the public has a need and right to make its own judgments with respect to banks." It is the goal of government regulation to protect customers from monopoly power and market concentration as banking organizations consolidate and move into new lines of business. Arguably, antitrust constraints prevent abuses of market power. Yet, current antitrust parameters and practices, at least as currently applied by the financial regulatory agencies, will not prevent the market leaders in San Diego, like BankAmerica, Union Bank, and Wells Fargo, from playing gatekeeper roles and controlling the essential bank networks or technological products.

The argument can be made that "for all the hand-wringing about megamergers, there will still be abundant choices for customers on the prowl. The combination of NationsBank and BankAmerica will create an enormous bank, but one that still will control only a little more than 8% of the nation's bank deposits."  

---

714. Boro, supra note 240, at 481 n.220.
APPENDIX A

SAN DIEGO MERGER TIME LINE—1986 to 1998

1986  WELLS FARGO BANK / CROCKER NATIONAL BANK
Wells Fargo Bank acquired Crocker National Bank. At the time of the merger, Wells Fargo operated 187 branches in Southern California. Crocker operated 319 branches in the state of California, 7 of these branches in San Diego County. Crocker had $19.2 billion in assets at the time of Wells Fargo’s acquisition.

1987  FIRST NATIONAL BANK / NATIONAL BANK, LA JOLLA /
NATIONAL BANK OF FAIRBANKS RANCH

1988  WELLS FARGO BANK / BARCLAYS BANK OF CALIFORNIA
Wells Fargo acquired Barclays Bank of California. At the time of acquisition Barclays had assets of $1.3 billion, but had no branch offices in San Diego.

1988  UNION BANK / CALIFORNIA FIRST BANK
San Francisco based Union Bank completed the acquisition of California First Bank in 1988. Shortly after the California First deal, true to its established mode of dealing with bank failures, “the FDIC entered into a purchase and assumption agreement with Union Bank which assumed all the insured deposits of Bank of Newport, after the California Superintendent of Banks closed and took possession on August 12, 1994 of Bank of Newport in Newport Beach, ordered that it be liquidated, and appointed the FDIC as receiver.”

1990  WELLS FARGO BANK / GREAT AMERICAN FIRST SAVINGS BANK
Wells Fargo began its purchase of the entire California retail branch network of Great American December 1, 1990, completing the initial purchase of 92 Southern California branches. The first-phase purchase

price was approximately $365 million for which Wells Fargo acquired assets with a Great American book value of $4.1 billion.\textsuperscript{721} In connection with the branch purchase, Wells Fargo also purchased $6.2 billion of deposits from Great American.\textsuperscript{722} Included in this purchase price were $3.7 billion of loans and deposit liabilities of $4.4 billion that were assumed by Wells Fargo.\textsuperscript{723} The purchase of the 38 remaining Great American branches was completed August 1, 1991.\textsuperscript{724} In connection with the second-phase purchase, Wells Fargo acquired assets with a Great American book value of $1.7 billion, including cash of $1.6 billion, and assumed deposit liabilities of $1.8 billion.\textsuperscript{725}

**1990 WELLS FARGO BANK / TORREY PINES BANK**  
Wells Fargo acquired Torrey Pines Group of Solana Beach and its subsidiary, Torrey Pines Bank.\textsuperscript{726} At the time of the acquisition, Torrey Pines Bank had assets of $443 million.\textsuperscript{727}

**1990 SECURITY PACIFIC NATIONAL BANK / LA JOLLA BANK & TRUST CO.**  
Security Pacific National Bank acquired La Jolla Bank & Trust Company.\textsuperscript{728}

**1991 BANK OF SAN DIEGO / BANK OF LA COSTA**  
The Bank of San Diego acquired the Bank of La Costa.\textsuperscript{729}

**1992 BANK OF SAN DIEGO / AMERICAN VALLEY BANK**  
The Bank of San Diego acquired American Valley Bank of El Cajon.\textsuperscript{730}

**1992 PENINSULA BANK / CITIZEN WESTERN BANK**  
Peninsula Bank acquired Citizen Western Bank of San Diego.\textsuperscript{731}

**1992 BANKAMERICA / SECURITY PACIFIC NATIONAL BANK**  

\textsuperscript{721.} See id.  
\textsuperscript{722.} See id.  
\textsuperscript{723.} See id.  
\textsuperscript{724.} See id.  
\textsuperscript{725.} See id.  
\textsuperscript{726.} See id.  
\textsuperscript{727.} See id.  
\textsuperscript{728.} See Mergers in California Since 1980, supra note 717.  
\textsuperscript{729.} See id.  
\textsuperscript{730.} See id.  
\textsuperscript{731.} See id.
1992 FIRST PACIFIC NATIONAL BANK / TEMECULA VALLEY NATIONAL BANK AND SAN MARCOS NATIONAL BANK
Escondido National Bank, Escondido, CA, acquired Temecula Valley National Bank and San Marcos National Bank, changing the name of the new combination to First Pacific National Bank.732

1993 GROSSMONT BANK / BANK OF SAN DIEGO
Grossmont Bank assumed the deposits of the San Diego County branches of the Bank of San Diego on October 29, 1993, and the Bank of San Diego was closed.

1993 FIRST INTERSTATE BANK / CALIFORNIA REPUBLIC BANK
California Republic Bank merged with and into First Interstate Bank of California on December 10, 1993, and California Republic Bank was closed.

1994 FIRST INTERSTATE BANK / SAN DIEGO TRUST AND SAVINGS BANK
First Interstate Bank of California acquired San Diego Trust & Savings Bank in 1994.733 At the time of regulatory approval, First Interstate had assets of $50.1 billion and San Diego Trust reported deposits of $1.8 billion.734

1995 FIRST PACIFIC NATIONAL BANK / OVERLAND BANK
First Pacific National Bank acquired Overland Bank, Temecula, CA.735

1996 FIRST NATIONAL BANK / BANK OF SOUTHERN CALIFORNIA
First National Bank of San Diego merged with Bank of Southern California, San Diego, CA.736

1996 UNION BANK / THE BANK OF CALIFORNIA
This combination made Union Bank the third largest commercial bank in California with $30.3 billion in assets.737

1996 WELLS FARGO BANK / FIRST INTERSTATE BANK
Wells Fargo & Co. completed its merger with First Interstate Bank during 1996, increasing Wells Fargo’s assets to $108.9 billion as of Decem-

732. See id.
733. See Mergers & Acquisitions: 12 First Quarter Actions Include Okay of Deal Once Denied Under CRA, 13 No. 8 BANKING POL’Y REP. 14 (Apr. 18, 1994).
734. See id.
735. See Mergers in California Since 1980, supra note 717.
736. See id.
ber 1996, from $50.3 billion in January 1996. Wells Fargo acquired assets with a First Interstate book value of approximately $55 billion, for a purchase price of $11.3 billion. In order to secure approval of the merger, the bank was required by regulatory agencies to divest itself of 61 branches to Home Savings of America and completed the divestiture September 1996. Wells Fargo was required to divest itself of 10 First Interstate branches, closed 40 more First Interstate branches, continuing to operate only 10 of the previous First Interstate branches in San Diego County.

1996 RANCHO VISTA NATIONAL BANK AND PACIFIC COMMERCE BANK OF CHULA VISTA / GB BANCORPORATION

Approval granted by the Federal Reserve Board December 18, 1996, under section 3 of the Bank Holding Company Act, for GB Bancorporation of San Diego (assets $527 million at the time of the acquisition), to acquire up to 24.9% of the voting shares of Rancho Vista National Bank (assets $93 million) of Vista (a suburb of San Diego) and Pacific Commerce Bank, of Chula Vista (also a suburb of San Diego).

1996 FIRST PACIFIC NATIONAL BANK / BANK OF RANCHO BERNARDO

First Pacific National Bank acquired the Bank of Rancho Bernardo.

1997 GREAT WESTERN BANK / WASHINGTON MUTUAL

Great Western agreed to be acquired by Washington Mutual in 1997. Washington Mutual now claims to be “the largest savings institution in the United States, with combined assets of more than $94 billion” as of August 1997 and “the [number one] mortgage lender on the West Coast.” Originally Great Western was a statewide savings institution, having only a minor presence in the San Diego financial market. On June 30, 1987, with 19 retail branches in San Diego County, the bank’s total assets were reported as approximately $24 billion, with total deposits of $17.7 billion. On July 1, 1997, the day the merger deal was closed, Washington Mutual had $46.1 billion in assets, Great Western reported assets of $42.9 billion.

739. See id. at 8.
740. See Mergers in California Since 1980, supra note 721.
741. Letter from Michael L. Amato, Senior Vice President of Great Western Bank to Great Western Customer (Oct. 17, 1997) (on file with author).
1998 **BANKAMERICA / NATIONSBANK**

On April 13, 1998, BankAmerica and NationsBank announced they will seek regulatory approval to merge. The combined banks will have $570 billion in assets. The Federal Reserve Board and the U.S. Justice Department gave regulatory approval for this $57.7 billion merger in August 1998. The boards of both banks approved the merger September 23, 1998. NationsBank had been the nation's third largest bank, BankAmerica the fifth largest.

1998 **BANK OF COMMERCE / RANCHO VISTA NATIONAL BANK**

Bank of Commerce acquired the assets of Rancho Vista National Bank in May 1998. As of April 30, 1998, the pro forma combined balance sheets of the two banks included $703 million in assets, $635 million in deposits, and $487 million in loans.

1998 **SUMITOMO BANK OF CALIFORNIA / GROSSMONT BANK OF SAN DIEGO AND FIRST PACIFIC NATIONAL BANK**

The combined banks will be renamed Bank of California, have assets of about $6 billion and 70 branch offices, making it the fifth largest commercial bank in the state.

1998 **PENINSULA BANK OF SAN DIEGO / WESTERN BANCORP**

July 24, 1998, Peninsula Bank and Western Bancorp announced they would merge. However, in September 1998, Peninsula Bank exercised their right to withdraw from the merger when the price of Western Bancorp common stock fell below $36.65 a share. With the addition of Norwest, Wells Fargo is the seventh largest in assets and the third largest in market value among U.S. bank holding companies.

1998 **GROSSMONT BANK / FIRST PACIFIC NATIONAL BANK**


1998 **GLENDALE FEDERAL BANK / CALIFORNIA FEDERAL BANK**

Glendale merged with California Federal in September 1998.

---

746. See id.
747. See id.
749. See Arthur Grupe, supra note 651, at 14.
751. See id.
752. See Mergers in California Since 1980, supra note 717.
Scripps Bank acquired Pacific Commerce Bank in November 1998.\textsuperscript{754}

In November 1998, Wells Fargo and Norwest announced the completion of a merger creating “the new Wells Fargo, a diversified financial services company.”\textsuperscript{755} The merger had been agreed to in June, and won the support of both boards and the stockholders in October.\textsuperscript{756} This combination raised Wells Fargo’s total assets to $196 billion, with almost 102,000 employees servicing 15 million customers through 5,836 locations.\textsuperscript{757}

\textsuperscript{753} See id.
\textsuperscript{754} See id.
\textsuperscript{756} See id.
\textsuperscript{757} See id.
## APPENDIX B
### CLOSING AND ASSISTANCE TRANSACTIONS IN SAN DIEGO COUNTY 1985-1996
#### BANK INSURANCE FUND
#### CLOSINGS & ASSISTANCE TRANSACTIONS IN SAN DIEGO COUNTY
Calendar Years 1985-1996

<table>
<thead>
<tr>
<th>NAME</th>
<th>LOCATION</th>
<th>DATE OF FAILURE</th>
<th>TRANSACTION TYPE</th>
<th>TOTAL DEPOSITS</th>
<th>TOTAL ASSETS</th>
</tr>
</thead>
<tbody>
<tr>
<td>California Heritage Bank</td>
<td>San Diego, CA</td>
<td>Nov. 22, 1985</td>
<td>P&amp;A</td>
<td>22,397</td>
<td>24,114</td>
</tr>
<tr>
<td>Balboa National Bank</td>
<td>San Diego, CA</td>
<td>Jan. 14, 1988</td>
<td>PO</td>
<td>29,391</td>
<td>29,316</td>
</tr>
<tr>
<td>Landmark Thrift &amp; Loan Assoc.</td>
<td>San Diego, CA</td>
<td>July 12, 1991</td>
<td>PO</td>
<td>15,835</td>
<td>16,638</td>
</tr>
<tr>
<td>First Western Bank, N.A.</td>
<td>San Diego, CA</td>
<td>April 15, 1993</td>
<td>P&amp;AI</td>
<td>15,313</td>
<td>16,235</td>
</tr>
<tr>
<td>First California Bank</td>
<td>La Mesa, CA</td>
<td>July 9, 1993</td>
<td>P&amp;AI</td>
<td>77,014</td>
<td>79,395</td>
</tr>
<tr>
<td>The Bank of San Diego</td>
<td>San Diego, CA</td>
<td>Oct. 29, 1993</td>
<td>P&amp;AI</td>
<td>289,131</td>
<td>294,277</td>
</tr>
</tbody>
</table>

A/A = Open Bank Assistance, FSLIC Rehabilitation  
P&A = Purchase & Assumption of Liabilities  
P&O = Payoff of Insured Deposits  
P&AI = Purchase & Assumption - Insured Deposits  

### APPENDIX B (cont’d)
SAVINGS ASSOCIATION INSURANCE FUND/FEDERAL SAVINGS & LOAN INSURANCE CORPORATION
CLOSINGS AND ASSISTANCE TRANSACTIONS IN SAN DIEGO COUNTY *

<table>
<thead>
<tr>
<th>NAME</th>
<th>LOCATION</th>
<th>DATE OF FAILURE</th>
<th>TRANSACTION TYPE</th>
<th>TOTAL DEPOSITS</th>
<th>TOTAL ASSETS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central Savings &amp; Loan Assoc.</td>
<td>San Diego, CA</td>
<td>May 31, 1985</td>
<td>A/A</td>
<td>1,680,711</td>
<td>2,308,903</td>
</tr>
<tr>
<td>Eureka Federal Savings &amp; Loan Assoc.</td>
<td>San Diego, CA</td>
<td>June 21, 1985</td>
<td>A/A</td>
<td>1,364,360</td>
<td>1,570,628</td>
</tr>
<tr>
<td>Seapointe Savings &amp; Loan Assoc.</td>
<td>Carlsbad, CA</td>
<td>May 31, 1986</td>
<td>PO</td>
<td>37,882</td>
<td>17,343</td>
</tr>
<tr>
<td>Sun Savings &amp; Loan Assoc.</td>
<td>San Diego, CA</td>
<td>July 18, 1986</td>
<td>A/A</td>
<td>334,444</td>
<td>370,935</td>
</tr>
<tr>
<td>Carver Savings &amp; Loan Assoc.</td>
<td>Escondido, CA</td>
<td>Jan. 27, 1989</td>
<td>PO</td>
<td>285,969</td>
<td>265,763</td>
</tr>
<tr>
<td>Great American First Savings Assoc.</td>
<td>San Diego, CA</td>
<td>Aug. 9, 1991</td>
<td>P&amp;A</td>
<td>7,230,789</td>
<td>9,523,603</td>
</tr>
<tr>
<td>Heartland Savings &amp; Loan Assoc.</td>
<td>La Mesa, CA</td>
<td>Sept. 6, 1991</td>
<td>P&amp;A**</td>
<td>121,671</td>
<td>120,790</td>
</tr>
<tr>
<td>Home Federal Savings &amp; Loan Assoc.</td>
<td>San Diego, CA</td>
<td>July 6, 1992</td>
<td>P&amp;A**</td>
<td>8,903,571</td>
<td>12,175,590</td>
</tr>
</tbody>
</table>

A/A = Open Bank Assistance, FSLIC Rehabilitation
P&A = Purchase & Assumption of Liabilities
PO = Payoff of Insured Deposits
P&AI = Purchase & Assumption—Insured Deposits
* The FDIC or FSLIC took control of the institution, operated the open institution prior to resolution.
** Placed in RTC conservatorship prior to resolution.

The Federal Deposit Insurance Corporation - Division of Research and Statistics