

**Texas
Sunset
Advisory
Commission**

STAFF EVALUATION

Banking Department

Savings and Loan Department

Office of Consumer Credit Commissioner

Finance Commission

Texas Library and Archives Commission

A Staff Report
to the
Sunset Advisory Commission



SAVINGS AND LOAN DEPARTMENT

FOREWORD

Over the past several years, there has been a sustained interest among the states in a new concept in legislative review popularly described as sunset. Since 1976, more than half the states have enacted legislation which embodies the primary element of sunset, the automatic termination of an agency unless continued by specific action of the legislature.

The acceptance of this concept has been aided by a general agreement that the normal pressures of the legislative process tend to prevent a systematic review of the efficiency and effectiveness with which governmental programs are carried out. The sunset process is, then, an attempt to institutionalize change and to provide a process by which a review and redefinition of state policy can be accomplished on a regular systematic basis.

The Texas Sunset Act (Article 5429K, V.A.C.S., as amended) was enacted by the 65th Legislature in 1977. Under the provisions of the Act, agencies are automatically terminated according to a specified timetable, unless specifically continued by the legislature.

To assist the legislature in making the determination of whether an agency should be continued and, if continued, whether modifications should be made to its operations and organizational structure, the Act establishes a ten-member Sunset Advisory Commission composed of eight legislative members and two public members. The commission is required to evaluate the performance of the agency in accordance with specific criteria set out in the Act and to recommend necessary changes resulting from the findings of the evaluation.

The process by which the commission arrives at its recommendations moves through three distinct phases beginning with a self-evaluation report made by the agency to the commission. The second phase involves the preparation of a report to the commission by its staff, evaluating the activities of the agency, and proposing suggested changes for commission consideration. The final phase involves public hearings on the need to continue or modify an agency and the development of commission recommendations and legislation, based on the agency self-evaluation, staff report, and public testimony.

The Sunset Commission's findings, recommendations, and proposed legislation are then required to be transmitted to the legislature when it convenes in regular session.

INTRODUCTION AND ORGANIZATION OF AGENCY REVIEW

The Texas Sunset Act abolishes this agency on September 1, 1983 unless it is re-established by the 68th Legislature.

The staff reviewed the activities of this agency according to the criteria set out in the Sunset Act and has based its conclusions on the findings developed under these criteria.

Taken as a whole, these criteria direct the review of an agency to answer four primary questions:

1. Does the state need to perform the function or functions under review?
2. Could the public still be adequately served or protected if the functions were modified?
3. Is the current organizational structure the only practical way for the state to perform the function?
4. If the agency is continued and continues to perform the same functions, can changes be made which will improve the operations of the agency?

The report is structured to present the performance evaluation of the agency. The application of the across-the-board recommendations developed by the commission to deal with common problems are presented in a chart at the end of the report and are not dealt with in the text except in one instance. When the review develops a position which opposes the application of a particular recommendation, the rationale for the position is set forth in the text.

SUMMARY OF STAFF FINDINGS AND CONCLUSIONS

SUMMARY

The Savings and Loan Department was created in 1961 and is currently active. The agency's major functions include: 1) the approval of applications for state chartered savings and loan associations; 2) the examination of all state chartered savings and loan associations and the monitoring of savings and loans with deficiencies; and 3) enforcement efforts directed toward violations of the Act or fraudulent practices.

The results of the review indicated that the department is generally operated in an efficient and effective manner. It was determined that sufficient reason exists for the state to continue to regulate the savings and loan industry in Texas; however the review showed that there are organizational alternatives to the current structure which could be considered. The review also indicated that if the department is continued, several modifications should be made to improve the efficiency and effectiveness of the agency's operations.

Approaches for Sunset Commission Consideration

I. MAINTAIN THE AGENCY WITH MODIFICATIONS

- A. Agency operations
 - 1. Overall administration
 - a. All agreements for the leasing of space by the department should be obtained through the State Purchasing and General Services Commission. (management improvement - non-statutory)
 - 2. Evaluation of programs
 - a. Rules and regulations defining the statutory criteria for chartering a new savings and loan association should be promulgated. (management improvement - non-statutory)
 - b. The department should adopt a policy of maintaining work-papers for at least five years and should request the destruction of all records in accordance with the provisions of Article 5441a, V.A.C.S.
 - c. The department should initiate an electronic data processing examination program for state chartered savings and loan associations. (management improvement - non-statutory)

- d. The agency should permit field examiners to submit hand-written copies of examination reports to the Austin office for final processing. (management improvement - non-statutory)
- e. Copies of complaints and the association's responses should be forwarded to the field examiner responsible for the examination of that savings and loan. (management improvement - non-statutory)
- f. The department should develop additional written policies concerning conflicts-of-interest for the agency's examiners. (management improvement - non-statutory)

II. ALTERNATIVES

A. Regulatory alternatives

1. Modify the hearing procedures for the chartering of state savings and loan associations. Under this approach, the role of the hearings officer in public hearings on new savings and loan charters would be expanded to include reporting to the commissioner with findings of fact based on evidence received at the hearing, including findings on each of the statutory criteria as well as underlying facts on which these findings are based. The review indicated that hearings examiners in other state agencies as well as in savings and loan regulatory agencies in other states act in this way. This alternative would provide the commissioner with a more manageable document for use in making chartering decisions and would allow the commission to benefit from an evaluation of the evidence by an impartial official who observed the presentation of testimony.
2. Instituting a shared examination program with the Federal Home Loan Bank Board. Under this approach, the Savings and Loan Department would share responsibility for the regulation of state chartered savings and loan associations with the Federal Home Loan Bank Board (FHLBB). The operation of a shared examination program would involve conducting examinations jointly with the FHLBB examiners or participating in an alternate year examination program. The review indicated that Texas is only one of five

states which conducts separate examinations. Instituting a shared examination program should reduce costs to both the federal and state agencies as well as the savings and loan associations regulated.

3. Granting the commissioner the power to approve the acquisition of 10 percent or more of the voting stock of a state chartered savings and loan association. Under this approach, the commissioner would be able to disapprove the acquisition of 10 percent or more of the voting stock of a state chartered savings and loan association in certain specified instances. This authority could be used to disapprove transfers of control where competition would be lessened; the financial stability of the savings and loan would be jeopardized or the association would become insolvent. The review indicated that granting the commissioner the authority to approve transfers of control is consistent with the authority granted the state banking commissioner, and other federal and state agencies regulating savings and loans.

AGENCY EVALUATION

The review of the current operations of an agency is based on several criteria contained in the Sunset Act. The analysis made under these criteria is intended to give answers to the following basic questions:

1. Does the policy-making structure of the agency fairly reflect the interests served by the agency?
2. Does the agency operate efficiently?
3. Has the agency been effective in meeting its statutory requirements?
4. Do the agency's programs overlap or duplicate programs of other agencies to a degree that presents serious problems?
5. Is the agency carrying out only those programs authorized by the legislature?
6. If the agency is abolished, could the state reasonably expect federal intervention or a substantial loss of federal funds?

BACKGROUND

Organization and Objectives

The first incorporated savings and loan associations in Texas were established in 1866. Prior to 1913, there were no general laws regulating savings and loan associations. The first legislation in Texas pertaining to the regulation of savings and loan associations was enacted in 1913 by the 33rd Legislature, in response to abuses within the industry including usurious interest charged to borrowers. These statutes gave the Secretary of State the authority to approve or reject applications to charter a savings and loan while the Commissioner of Insurance and Banking was given the responsibility for supervising the operations of the associations.

In 1923, in response to concerns that the Department of Banking and Insurance was too large and diverse for one individual to administer, separate agencies for banking and insurance were created. Since the statute failed to mention the disposition of savings and loan associations specifically, these institutions continued to be regulated by the Insurance Commissioner. Between 1922 and 1928, the number of savings and loan associations increased rapidly, and with that increase, came regulatory problems; chief among these being the inability of the commissioner to prevent the organization of associations which should not have been chartered. These problems were addressed by the 41st Legislature in 1929 which recognized that savings and loan associations had increasingly come to resemble banks and to require a type of examination similar to that applied to banks. In 1929, the statutes were changed to transfer the regulation of savings and loan associations to the Banking Commissioner and to authorize the commissioner to investigate the character and general fitness of proposed incorporators and to consider public convenience and the potential for the successful operation of the proposed association. It also extended the supervisory powers of the Banking Commissioner over savings and loan associations.

Beginning in 1946, the Texas savings and loan industry again experienced rapid growth. The number of state chartered associations increased from 51 to 196 between 1946 and 1970. The demand for the financing of new as well as older home purchases gave added emphasis to the rapid growth of the savings and loan industry. To meet the needs of this rapidly growing industry, the legislature, in 1961, created a separate Savings and Loan Department.

The Savings and Loan Commissioner is charged with the responsibility of administering and enforcing the provisions of the Texas Savings and Loan Act and is appointed by and serves at the pleasure of the Finance Commission. The agency is financed with fee income deposited to an operating account outside the state treasury or invested in interest-bearing accounts. For calendar year 1982, the agency has a staff of 42 and an operating budget of \$2,116,600.

Regulation of the savings and loan industry takes the general form used by most states. As of December 31, 1981, there were 251 state chartered and 65 federally chartered savings and loan associations operating in Texas with assets totalling \$29.6 billion and \$8.5 billion, respectively. The department is responsible for carrying out the policy directives and rules adopted by the Finance Commission and the savings and loan section of the commission and for administering the Texas Savings and Loan Act which provides for the chartering and regulation of all state chartered associations doing business in the state.

The Savings and Loan Department is not the only government agency regulating savings and loan associations in Texas. The federal government also takes an active role, both as an examiner of savings and loan associations and as an insurer of depositor's accounts. The federal role began in 1932, when a system of federally chartered savings institutions was established. The Federal Home Loan Bank Board (FHLBB) administers this system. The board grants charters, examines and supervises federally chartered associations and serves as a central credit facility lending money to member institutions. The board also directs the activities of the Federal Savings and Loan Insurance Corporation (FSLIC) which insures accounts up to \$100,000. All federal savings and loan associations are required by law to be insured by the FSLIC. State chartered institutions that apply for insurance and meet the board's eligibility requirements are granted similar protection. In Texas, all but two associations including both federally and state chartered associations are insured. All state chartered savings and loans insured by the FSLIC are subject to periodic examination by the Federal Home Loan Bank Board as well as by the Savings and Loan Department.

The major areas of responsibility of the Savings and Loan Department include: 1) the approval of applications for state chartered savings and loan associations; 2) the examination of all state chartered savings and loan associations and the monitoring of savings and loans with deficiencies; and 3) enforcement efforts directed toward violations of the Act or fraudulent practices.

Under the Texas Savings and Loan Act, any five or more citizens of the state may incorporate a savings and loan association. Incorporators must file with the commissioner an application for charter and the articles of incorporation containing basic information about the proposed savings and loan; proposed by-laws and rules for its operations; biographical information and letters of character reference concerning each of the directors; and a statement of subscribers to the capital stock, if any, of the proposed savings and loan. The Act specifies that applications for a savings and loan charter be granted when the following criteria are satisfied:

1. The character, responsibility and general fitness of the proposed officers and directors are such as to ensure that the association will be honestly and efficiently conducted;
2. The proposed association will have qualified full-time management;
3. There is a public need for the proposed association;
4. The volume of business will support the profitable operation of the association; and
5. The operation of the association will not unduly harm any existing association.

Texas law permits associations to be organized as either stock associations or mutual associations. In a stock association, shareholders or stockholders contribute permanent capital to the association in exchange for ownership interests, whereas in a mutual association the capital is "lent" to the association by its members or savings customers. The issuance of capital stock offers an additional avenue of increasing a savings and loan's net worth not available to mutual associations. While nationally over 80 percent of all savings and loan associations are mutuals, about 71 percent of the associations in Texas are stock associations. Although the statute specifies minimum capital requirements for stock associations based on the population of the community where the home office is to be located, capitalization is effectively controlled by the FSLIC through approval of insurance of accounts. Associations generally do not begin operations with less than \$500,000 capitalization, and those in large metropolitan areas usually require at least \$2 million. The review indicated that between 1979 and 1981, only 11 applications for new charters were received and 10 were approved. The commissioner is also authorized to approve applications for additional branches, relocations, name changes, mergers, acquisitions and consolidations.

Each of the 251 savings and loan associations chartered under state law is required by statute to be examined at frequent intervals by the department. The review indicated that examinations occur approximately every 18 months unless the association is experiencing financial difficulty thus requiring more frequent examinations. State examiners focus on determining the solvency and profitability of the association, the quality of loans and investments, the adequacy of general operations and the performance of management. After the examination is completed, an exit conference is conducted with the association's board of directors to discuss the examiner's findings and any recommendations for corrective action. A written exam report including a general statement of the affairs of the savings and loan is prepared, and a copy is furnished to the association's board. A computerized monitoring system assists the department's staff by providing the current financial status of regulated associations. In 1981, the department examined 206 savings and loan associations.

A range of enforcement powers is available to the agency in meeting violations of the law or regulations and unsafe or unsound practices. In most cases, where a problem has been discovered during an examination and certain remedial actions are recommended to the board of directors, the response of the board in taking corrective measures is sufficient and no further actions are required by the department. When a savings and loan fails to take corrective action, the commissioner can demand that the practices or violations be discontinued, and if stronger action is required, issue a formal cease and desist order. If problems persist, because of refusal to comply with a cease and desist order or other violations, the commissioner may issue an order removing from office or employment an officer or director. In connection with a cease and desist order and with the consent of a majority of the board members, the commissioner may also request that the association be placed under the supervisory control of the commissioner. A supervisory agent is then appointed by the commissioner to supervise and monitor the operations of the association. Finally, when the interests of members and creditors of an association are seriously jeopardized through insolvency or a substantial dissipation of assets, the commissioner can apply to the district court for appointment as receiver. The receiver immediately takes charge of the affairs of an association, subject to the direction of the court, and manages the savings and loan and takes steps to conserve the assets and protect the rights of creditors of the association and its members. The review

indicated that in most instances the savings and loan association voluntarily takes action to correct deficiencies; the commissioner issued only 16 cease and desist orders between 1979 and 1982. There were 12 cases of supervision or conservatorship of savings and loan during the same period of time.

Enforcement activities of the agency also involve investigating and resolving consumer complaints. The agency generally acts as a liaison between the complainant and the association concerned. In calendar year 1981, the agency received 605 complaints, all of which were resolved informally.

The review and evaluation of the Savings and Loan Department indicated that its regulatory activities generally serve to ensure an adequate level of public protection. However, the review did show that modifications in a number of areas would increase the efficiency and effectiveness of agency operations. Results of the evaluation follow.

REVIEW OF OPERATIONS

The evaluation of the operations of the Savings and Loan Department is divided into general areas which deal with: 1) a review and analysis of the policy-making body to determine if it is structured so that it is fairly reflective of the interests served by the agency; and 2) a review and analysis of the activities of the agency to determine if there are areas where the efficiency and effectiveness can be improved both in terms of the overall administration of the agency and in the operations of specific agency programs.

Policy-Making Structure

In general, the structure of a policy-making body should have as basic statutory components, specifications regarding the composition of the body and the qualifications, method of selection, and grounds for removal of the members. These should provide executive and legislative control over the organization of the body and ensure that members are competent to perform required duties, that the composition represents a proper balance of interests affected by the agency's activities, and that the viability of the body is maintained through an effective selection and removal process.

The Savings and Loan Department operates under the direction of the Finance Commission. Within the commission there is a three-member savings and loan section. Two members of this section must be savings and loan executives and the third member is appointed on the basis of recognized business ability. Primary responsibilities of the section include advising the commissioner on the department's operations and promulgating rules and regulations concerning state chartered savings and loan associations. Recommended changes concerning the savings and loan section are addressed in the report on the Finance Commission.

Overall Administration

The evaluation of the overall administration of the agency focused on determining whether the operating policies and procedures of the agency provide a framework which is adequate for the internal management of personnel and funds, and which satisfies reporting and management requirements placed on the agency and enforced through other state agencies.

The objectives of the administrative activities of the agency include: 1) directing and supervising the administration of the Savings and Loan Act; 2) managing agency personnel records, purchasing, inventory, data processing and

deposits and investment of revenue; and 3) budgeting for the agency. The results of the evaluation indicated that the agency is generally administered in an efficient manner. The review showed that although agency revenues are not deposited to the state treasury, the agency is generally in compliance with the requirements placed on agencies controlled through the appropriations process. In addition, analysis of the agency's investment policies indicated that the department has maximized the yield on its investments through efficient money management practices. However, one area of concern was identified in the review. The Savings and Loan Department currently leases office space from University Savings Association of Austin, based on a lease agreement dated July 30, 1976. The original lease was not obtained through competitive bidding nor was it secured by the State Purchasing and General Services Commission. The lease has been extended for two additional years beyond its original terms despite objections from the State Purchasing and General Services Commission which has informed the department that such a lease was not valid because it was at variance with Article 601b, V.A.C.S. This violation has also been cited by the State Auditor in his management letter for the last three years. The review showed that while the department recognized the need to renegotiate the lease, it has indicated that the primary goal of the agency is to purchase a building and they do not wish to be confined by a lease. Nevertheless, the review did not identify any reason why the agency could not and should not comply with the general law concerning leasing of space by state agencies until such time as space is purchased.

Evaluation of Programs

The review of the agency's program activities focused on the extent to which these activities achieve the objectives of the Texas Savings and Loan Act: to protect the public from unlawful and unsafe practices in the savings and loan industry by examining and supervising state chartered savings and loan associations. The review also sought to determine if areas exist where the efficiency and effectiveness of the operations could be improved.

Chartering Savings and Loan Associations

The Texas Savings and Loan Act requires that savings and loan associations be chartered. Under the Act, any five or more Texas citizens may incorporate a savings and loan by filing with the commissioner the following information: 1) the articles of incorporation containing basic information about the proposed association; 2) proposed bylaws and rules for the association's operation; 3) biographical

information and letters of character reference concerning each of the directors; and 4) a statement of subscribers to the capital stock, if any, of the proposed savings and loan. Charters are granted when specified statutory criteria concerning the fitness and character of the proposed organizers and management, the need for the association, and the harm to existing associations have been satisfied.

The review of the chartering activities of the Savings and Loan Department included an evaluation of the criteria applied by the commissioner in approving applications; the appropriateness of procedures governing charter application hearings; and the consistency and objectivity reflected in charter approvals. The results of the review indicated that the chartering function is generally conducted in an efficient and effective manner. However, one area of concern was identified where needed changes would provide greater notice to the public and assist the commissioner in ensuring consistency in the review of new savings and loan charter applications.

Definitions of Chartering Criteria. The review indicated that specific standards for use in evaluating savings and loan charter applications is especially important to ensure that the approval process is consistent and fair, offering all applicants an equal opportunity to obtain a charter. The Savings and Loan Act specifies a number of findings that must be made in order for an application to be approved: 1) the character, responsibility and general fitness of the proposed officers and directors are such as to ensure the association will be honestly and efficiently conducted; 2) the proposed association will have qualified full-time management; 3) there is a public need for the proposed association; 4) the volume of business will support the profitable operation of the organization; and 5) the operation of the association will not unduly harm any existing association. Although these statutory criteria are the basis for the determination by the commissioner as to whether a charter application will be approved or denied, these criteria have never been defined in rules and regulations. The promulgation of rules and regulations providing guidelines for use in determining whether the criteria have been met would provide adequate notice to both potential incorporators of state chartered savings and loan associations concerning how the Savings and Loan Act is interpreted, and would ensure fairness and consistency in the charter approval process.

Examination and Monitoring

State chartered savings and loan associations are required by statute to be reviewed by the department at frequent intervals. The review indicated that examinations occur approximately every 18 months depending on the financial status of the association. The examination assesses the association's compliance with laws and regulations as well as evaluating the solvency and profitability of an association, the quality of loans and investments, the adequacy of general operations and the performance of management. A written examination report, including the examiner's findings and any corrective action, is prepared and is furnished to the association's board of directors.

Agency monitoring of savings and loan associations with problems involves several activities. In addition to regular annual examinations, associations experiencing difficulties may be subject to a follow-up examination. The agency also monitors the financial condition of all savings and loans on the basis of information supplied monthly by associations. The financial information contained in these reports is then placed on computer and analyzed by the agency's staff. Monitoring activities may also involve requiring savings and loans with serious deficiencies to submit additional special reports detailing actions to correct the specific problems identified. Currently, 57 savings and loans are classified as problem associations and subject to special reporting requirements.

In assessing the efficiency and effectiveness of the examination function, the review covered a number of areas including: 1) the degree of supervision and control over examiners in the field; 2) the system of communication between the field and central office; 3) examination procedures and documentation procedures; 4) format and quality control of the examination report; 5) the method of establishing examination fees; and 6) procedures for follow-up action on the discovery of violations or abuses. Results of the review indicated that the agency is generally performing adequately in each of these areas. However, several concerns were noted where changes would increase the efficiency and effectiveness of the examination activity.

Retention of Workpapers. The review showed that the agency currently destroys the workpapers associated with the examination of a savings and loan after the next examination. Article 5441a, V.A.C.S. prohibits the destruction of public records without the the approval of the State Librarian and, in the case of financial records, the State Auditor. A review of the agency's applications for the

destruction of records between 1974 and 1982, indicated only one request for the destruction of workpapers since 1977. Prior to that time, the records appear to indicate that workpapers were maintained for at least five years. The review indicated that the department should adopt a policy of maintaining workpapers for at least five years and should request the destruction of all records in accordance with the provisions of Article 5441a, V.A.C.S.

Electronic Data Processing Examinations. The review showed that the Savings and Loan Department does not have the capability to review the electronic data processing (EDP) facilities of state chartered savings and loan associations or to examine association records maintained on EDP systems. A survey of other financial regulatory agencies in Texas, at the federal level, and in 15 selected states indicated that examination of EDP facilities in financial institutions is generally a part of the regular examination or done separately. Problems often identified by EDP examinations include: 1) inadequate planning of data processing acquisitions and conversions; 2) the failure of institutions to monitor the cost and performance of data processing systems; 3) inadequate security and control safeguards; and 4) failure to audit and reconcile data contained in the system. Acquiring personnel trained in electronic data processing examinations or providing EDP training for the agency's current examination staff, will permit savings and loan examiners to expand the scope of their examination and to ensure that the data maintained in EDP systems is valid and subject to sufficient controls.

Processing of the Examination Report. The review indicated that once an examination of a savings and loan is completed, the examination report is either typed by the field examiner or by clerical personnel at the savings and loan being examined, and is submitted in final form to the agency's office in Austin. Permitting the examiner to submit handwritten copies of the examination reports would eliminate the need for professional staff to spend extensive time performing clerical functions and the need to use non-agency staff in the preparation of the report thus increasing the efficiency of the examination process.

Enforcement

The objective of agency enforcement activities is to prevent or halt violations of law or regulations, and unsafe or improper activities. Where problems or abuses are discovered in the course of an examination, the savings and loan is notified of the violations and, when appropriate, allowed an opportunity to correct the problems. When problems persist, the commissioner may find it

necessary to meet personally with the association in an effort to resolve the problem. If stronger enforcement action is required, he may issue a cease and desist order. If problems continue, because of refusal to comply with the order or other violations, the commissioner may issue an order removing from office or employment an officer or director of the association or request that the board of directors consent to placing the association under the supervisory control of the commissioner. Finally, when the interests of the members and creditors of an association are seriously jeopardized, the commissioner can apply to the district court for appointment as receiver. The review indicated that in most instances the savings and loan association voluntarily takes action to correct deficiencies; the commissioner issued only 16 cease and desist orders between 1979 and 1982. There were only 12 instances of supervisory control over associations being exercised by the commissioner during this same period.

Enforcement activities of the agency also involve investigating and resolving consumer complaints. The agency received more than 600 complaints in 1981, all of which were resolved informally. The review indicated that agency enforcement efforts generally serve to ensure an adequate level of public protection. However, several changes concerning the handling of complaints were identified which would strengthen the agency's enforcement efforts.

Results of a questionnaire mailed to individuals who filed complaints with the department indicated substantial dissatisfaction with the agency's response to complaints, particularly in two areas: 1) agency's efforts in keeping complainants adequately informed of the status of their complaints; and 2) the department's efforts to investigate telephone complaints. The review also indicated that a log of telephone complaints is not maintained. The Sunset Commission has developed across-the-board recommendations for the handling of complaints which directs the agency to keep an information file concerning each written complaint received and to keep complainants periodically informed of the status of their complaints.

Another problem identified concerns providing field examiners with information on complaints filed against savings and loans. The review indicated that the agency's enforcement efforts would be strengthened if copies of complaints and the association's responses were consistently forwarded to examiners. This procedure would provide examiners with additional information concerning weaknesses in the association's operations which could be addressed during the regular examination.

Finally, a review of complaints filed with the agency indicated that almost half of the complaints filed concerned the handling of escrow accounts by savings and loans. In a number of instances, property taxes were paid by the association too late for taxpayers to qualify for a deduction on their current year's income taxes. The agency indicated that it is aware of the problem and has met informally with associations having consistent problems in this area in an effort to remedy the problem.

EVALUATION OF OTHER SUNSET CRITERIA

The review of the agency's efforts to comply with overall state policies concerning the manner in which the public is able to participate in the decisions of the agency and whether the agency is fair and impartial in dealing with its employees and the general public is based on criteria contained in the Sunset Act.

The analysis made under these criteria is intended to give answers to the following questions:

1. Does the agency have and use reasonable procedures to inform the public of its activities?
2. Has the agency complied with applicable requirements of both state and federal law concerning equal employment and the rights and privacy of individuals?
3. Has the agency and its officers complied with the regulations regarding conflict of interest?
4. Has the agency complied with the provisions of the Open Meetings and Open Records Act?

EVALUATION OF OTHER SUNSET CRITERIA

The material in this section evaluates the agency's efforts to comply with the general state policies developed to ensure: 1) awareness and understanding necessary to have effective participation by all persons affected by the activities of the agency; and 2) that agency personnel are fair and impartial in their dealing with persons affected by the agency and that the agency deals with its employees in a fair and impartial manner.

Open Meetings/Open Records

Review of the agency's compliance with the Open Meetings Act indicates that the agency has generally made timely filings with the Secretary of State's Texas Register Division providing appropriate notice of its meetings. However, the review did identify one concern relating to the savings and loan section's compliance with statutory requirements for executive sessions which is addressed in the report on the Finance Commission. The review of the agency's compliance with the Open Records Act indicated that the Savings and Loan Act makes reports of examinations and any information concerning the private business or affairs of individual associations confidential. Information concerning savings and loans considered open to the public by the agency include profit and loss statements, association bylaws, and some correspondence.

EEOC/Privacy

A review was made to determine the extent of compliance with applicable provisions of both state and federal statutes concerning affirmative action and the rights and privacy of individual employees. The Savings and Loan Department is operating under a recently revised affirmative action plan which includes formal grievance procedures and personnel selection policies. The results of the review indicates the agency performs adequately in this area.

Public Participation

In general, the review of public participation consists of an evaluation of the extent to which persons served by the programs and the general public have been kept informed of program activities, and the extent to which the program is responsive to the changing demands and needs of the public. The review indicated the agency does little in the way of public participation other than informing the general public of commission meetings through the Texas Register. In response to

problems resulting from the low visibility of regulatory agencies, the Sunset Commission has developed an across-the-board approach requiring the agency to prepare information of consumer interest describing the regulatory functions of the agency and to require licensees to display signs which inform consumers of the licensing agency's responsibilities.

Conflicts of Interest

Under state law, appointed state officers are subject to statutory standards of conduct and conflict of interest provisions. This includes, in certain circumstances, the filing of financial disclosure statements with the Office of Secretary of State. A review of the documents filed with the Secretary of State indicates that the Savings and Loan Commissioner has filed adequate financial statements. The review also showed that the agency has procedures for making employees aware of their responsibilities under general conflict of interest statutes. Employees who are responsible for the examination and supervision of savings and loan associations are also subject to a written department policy which prohibits examiners from obtaining credit from state chartered associations unless exempted by the director of examinations. The review indicated that, in order to provide maximum protection against conflict of interest problems, the department should also develop written policies similar to those required of state bank examiners concerning: the employment of spouses by state chartered savings and loan associations; indebtedness or ownership by a spouse to a state regulated savings and loan; and examination assignments in savings and loans where an examiner has previously worked or in which his or her family has an interest.

**NEED TO CONTINUE AGENCY FUNCTIONS
AND
ALTERNATIVES**

The analysis of the need to continue the functions of the agency and whether there are practical alternatives to either the functions or the organizational structure are based on criteria contained in the Sunset Act.

The analysis of need is directed toward the answers to the following questions:

1. Do the conditions which required state action still exist and are they serious enough to call for continued action on the part of the state?
2. Is the current organizational structure the only way to perform the functions?

The analysis of alternatives is directed toward the answers to the following questions:

1. Are there other suitable ways to perform the functions which are less restrictive or which can deliver the same type of service?
2. Are there other practical organizational approaches available through consolidation or reorganization?

NEED

The analysis of need and alternatives is divided into: 1) a general discussion of whether there is a continuing need for the functions performed and the organizational setting used to perform the functions; and 2) specific discussion of practical alternatives to the present method of performing the functions or the present organizational structure.

Function

After reviewing the basic sunset questions relating to need for a function, it was determined that sufficient reason exists for the state to regulate the savings and loan industry in Texas. The reasons for this determination are summarized in the material set out below.

Danger to the Public Sufficient to Warrant Regulation. In determining the need for regulation of the savings and loan industry in Texas, an analysis was made of: 1) whether the conditions that led to regulation of the industry in 1913 still exist; and 2) the possible harm to the public in the absence of regulation.

Although the first savings and loan associations in Texas were established in 1866, they were not subject to state regulation until 1913. Regulation was initiated at that time in response to abuses within the industry including usurious interest charged to borrowers. This long history of regulation of savings and loan associations as well as other financial institutions in this state reflects the quasi-public nature of these institutions. Since state chartered savings and loan associations in Texas hold savings totalling more than \$22 billion, assuring the soundness of these institutions through close regulation and supervision has long been in the public interest. As the number of savings and loans increased along with the volume of business in the industry, the need for more comprehensive regulation has continued to be recognized by subsequent amendments to the original Act. These amendments created a separate regulatory agency and have extended the supervisory powers of the commissioner in order to provide increased scrutiny of savings and loan operations.

In assessing the current need to continue to regulate the savings and loan industry, which includes 251 institutions and 1,288 branches, a number of factors were examined. Because every state regulates its savings and loan industry, the review could not compare regulated states with non-regulated ones. An assessment of the continuing need and the potential harm to the public if there were no

regulation of the industry was made, however, by examining the evidence of abuses which the current activities of the agency prevent or address. The review indicated that common problems identified during the examination process include deficiencies in loss reserve requirements, uncollateralized or improper loans (especially those made to savings and loan officers and directors) and questionable investment practices.

Another possible indication of potential harm are the types of complaints received from the public. Agency records show the department received 605 complaints in 1981. The agency staff investigates and informally resolves complaints of such problems as payments not being made on time from escrow accounts, excessive or miscalculated interest rates, and the improper assessment of late charges.

The evidence of current problems addressed by the agency's program of examination and supervision demonstrates that considerable potential harm to the public still exists. In the absence of regulation of the industry, it is unlikely that the possible harm would diminish, and in fact, it would likely increase without the deterrent effect of regulation in view of the increase in competitive pressures, the growing complexity of financial transactions, and the increasingly volatile economic climate.

Based on the analysis of need, it was determined that the need to perform many of the functions assigned to the Savings and Loan Department still exists; however, alternatives to the agency's current procedures have been identified. Alternatives to the current agency structure are discussed in detail in the report on the Finance Commission.

ALTERNATIVES

Regulatory Alternatives

Modifying the hearing procedures for the chartering of savings and loan associations. The Savings and Loan Act currently requires that prior to the commissioner's final decision to grant or deny a charter application, a public hearing must be held. The hearing, governed by provisions of the Administrative Procedure Act, provides opportunity for applicants, or any opposing parties, to present evidence as to whether the statutory conditions for approval of a charter exist. Applicants and opponents, both generally represented by counsel, can call and examine witnesses, cross-examine witnesses of the opposing party, and offer supporting reports or documents as evidence. A full transcript of the hearing, taken by a court reporter, is provided to the commissioner for use in making the determination to grant or deny a charter. Although a hearings officer, who is an attorney on the Savings and Loan Department's staff, conducts the hearings and rules on evidentiary matters, he makes no report of findings nor recommendations to the commissioner. The review indicated that benefits could be achieved by expanding the role of the hearings officer to include reporting to the commissioner with findings of fact based on evidence received at the hearing, including findings on each of the statutory criteria, as well as underlying facts on which those findings are based.

A review of the hearings process as it operates at the Public Utilities Commission and the Insurance Board, indicated that in both cases, the hearings officer or examiner who conducts the hearing prepares a proposal for decision, or report and proposed order, containing findings of fact concerning the application as well as conclusions of law, or recommendations as to the final determination to be made. In addition, a review of other states showed that in almost every case where a hearings officer conducted a hearing in lieu of the board or official responsible for making the final determination, the hearings officer made findings of fact concerning the application.

The review indicated that expanding the role of the hearings officer to include preparation of a report to the commissioner could result in increased efficiency in the chartering process, and promote consistent and fair charter decisions. The commissioner would be provided with a more manageable document for use in making the final decision to approve or deny, as compared to the current

transcripts of testimony which average 400 pages. In addition, the commissioner would benefit from an evaluation of evidence by an impartial official who observed the presentation of testimony.

Instituting a shared examination program with the Federal Home Loan Bank Board. All but two of the state chartered savings and loan associations in Texas are insured by the Federal Savings and Loan Insurance Corporation (FSLIC). As a result, these savings and loans are subject to periodic examination by the Federal Home Loan Bank Board (FHLBB) as well as the Savings and Loan Department.

Unlike the Banking Department which currently shares the responsibility for the examinations of state chartered banks with the federal regulatory agencies responsible for insuring these banks, the Savings and Loan Department examines all state chartered savings and loan associations independently of the Federal Home Loan Bank Board. The review indicated that Texas, which discontinued a joint examination program with the FHLBB ten years ago, is currently only one of five states conducting separate examinations. Participating in a coordinated examination program with the FHLBB that involves either conducting examinations jointly with the board's examiners, or participating in an alternate year examination program, would reduce costs to both federal and state agencies as well as the savings and loan associations regulated.

Grant the commissioner the power to approve the acquisition of 10 percent or more of the voting stock of a state chartered savings and loan association. Currently, the Savings and Loan Act authorizes the savings and loan section to promulgate rules and regulations to require associations to report to the commissioner any change in the control of an association involving more than 25 percent of the voting stock. However, the rules adopted by the section require reporting to the commissioner for changes in control involving more than 10 percent of the voting stock of an association. The review indicated that, unlike the banking commissioner, the savings and loan commissioner cannot disapprove of the transfers of control in instances where: 1) the acquisition would substantially lessen competition; 2) the poor financial condition of the acquiring party might jeopardize the financial stability of the savings and loan being acquired; 3) the experience, ability or integrity of the applicant is such that the acquisition might not be in the best interests of the association; or 4) the savings and loan would not be solvent. A survey of other agencies regulating savings and loans indicated that the Federal Home Loan Bank Board as well as more than half of the state agencies

surveyed also have the right to approve changes in control. Amending the Savings and Loan Act to provide the commissioner with the authority to approve the acquisition of 10 percent or more of the voting stock of a state chartered savings and loan, would make the statute consistent with the policy adopted by the savings and loan section and provide the commissioner with the authority to regulate changes in the control of associations comparable to that provided for the regulation of other financial institutions, within the state, at the federal level and in other states.

ACROSS-THE-BOARD RECOMMENDATIONS

SAVINGS AND LOAN DEPARTMENT

Applied	Modified	Not Applied	Across-the-Board Recommendations
A. ADMINISTRATION			
X		X	1. Require public membership on boards and commissions. 2. Require specific provisions relating to conflicts of interest.
		X	3. A person registered as a lobbyist under Article 6252-9c, V.A.C.S., may not act as general counsel to the board or serve as a member of the board.
		X	4. Appointment to the board shall be made without regard to race, creed, sex, religion, or national origin of the appointee.
		X	5. Per diem to be set by legislative appropriation.
		X	6. Specification of grounds for removal of a board member.
X			7. Board members shall attend at least one-half of the agency board meetings or it may be grounds for removal from the board.
X			8. The agency shall comply with the Open Meetings Act, and the Administrative Procedure and Texas Register Act.
X			9. The board shall make annual written reports to the governor and the legislature accounting for all receipts and disbursements made under its statute.
	X		10. Require the board to establish skill oriented career ladders.
X			11. Require a system of merit pay based on documented employee performance.
X*			12. The state auditor shall audit the financial transactions of the board during each fiscal period.
X			13. Provide for notification and information to the public concerning board activities.
X			14. Require the legislative review of agency expenditures through the appropriation process.

*Already in statute

Savings and Loan Department
(Continued)

Applied	Modified	Not Applied	Across-the-Board Recommendations
			B. LICENSING
		X	1. Require standard time frames for licensees who are delinquent in renewal of licenses.
		X	2. A person taking an examination shall be notified of the results of the examination within a reasonable time of the testing date.
		X	3. Provide an analysis, on request, to individuals failing the examination.
X			4. (a) Authorize agencies to set fees. (b) Authorize agencies to set fees up to a certain limit.
		X	5. Require licensing disqualifications to be: 1) easily determined, and 2) currently existing conditions.
		X	6. (a) Provide for licensing by endorsement rather than reciprocity.
		X	(b) Provide for licensing by reciprocity rather than endorsement.
		X	7. Authorize the staggered renewal of licenses.
			C. ENFORCEMENT
		X	1. Authorize agencies to use a full range of penalties.
X			2. Require files to be maintained on complaints.
X			3. Require that all parties to formal complaints be periodically informed in writing as to the status of the complaint.
		X	4. Specification of board hearing requirements.
			D. PRACTICE
		X	1. Revise restrictive rules or statutes to allow advertising and competitive bidding practices which are not deceptive or misleading.
		X	2. The board shall adopt a system of voluntary continuing education.