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MEMORANDUM

To: John Grant, President
UFCW Local 770

From: George M. Yin GMY

Re: Public Bank Proposals and City Charter Compliance

File No.: UFC3327.003

Date: June 16, 2020

I. *Introduction*

Recent events, including the COVID-19 pandemic, have illustrated the need for nimble banking responses that can quickly offer meaningful financial support to spur economic development and recovery. The City of Los Angeles, under the leadership of the City Council and Mayor, should act to strengthen the City's financial system to deliver needed support for the City's struggling communities. The recent enactment of AB 857 has delineated a clear path for cities to establish public banks. A public bank may be initiated by the City and added to the network of institutions that the City uses to perform particular financial services.

At the request of UFCW Local 770, we have prepared this memorandum to address concerns that certain provisions of the City Charter might impede such an effort. As discussed below, under the statutory scheme enacted by AB 857, the establishment of a public bank by the City need not be unduly delayed by seeking voter approval at a future election, nor is an amendment to the City Charter required to proceed.

II. *Background*

Since the 2007-08 financial crisis, a growing interest in public banking has sparked legislation and studies in state and local governments around the United States. For several years, the City Council has expressed an interest in public banking and has directed staff to review legal and feasibility issues with respect to establishing a public bank in the City. Until recently, various legal hurdles, the lack of clear legislative guidance, and practical concerns impeded the establishment of a public bank in the City. However, in October 2019, the Legislature adopted (and the Governor approved) AB 857, a new set of laws providing a clear process for the establishment of public banks by local agencies, subject to approval by the California Department of Business Oversight (DBO) and the Federal Deposit Insurance Corporation (FDIC).

Although the legal and procedural regime set forth in AB 857 removed legal uncertainties and established a clear path for public banks to be created by both general law and charter cities, a report from the Chief Legislative Analyst's Office dated February 27, 2020 (Assignment No: 20-02-0194) stated that in order for the City to form a public bank, a ballot measure to obtain

approval from the voters (and possibly to amend the City Charter) is needed before an application may be submitted. Specifically, the CLA concluded the following:

- A public bank would be considered "purely commercial" and would therefore require voter approval per the City Charter.

- Changes to the City Treasurer's "fiduciary authority or depository options" would require an amendment to the City Charter.

We have reviewed these conclusions and believe that a ballot measure is not necessary in light of AB 857's provisions.

III. *Public Banks are Not "Purely Commercial Enterprises;" Thus, an Application to Form a City Public Bank Does Not Require Voter Approval*

According to AB 857, before applying to form a public bank, a local agency must receive voter approval, unless the local agency is a charter city. (Cal. Gov't Code § 57606(c)(2) & (4).) As a charter city, Los Angeles is exempt from this requirement. However, the CLA's Report dated February 27, 2020 asserts that the Los Angeles City Charter requires "that a decision to form a public bank would require a ballot measure to obtain approval from the voters to move ahead with bank formation." (CLA's Report dated 2/27/20, at p. 1.) As discussed below, our own review shows that such voter approval is unnecessary under the process enacted by AB 857.

The City Charter provision in question, Section 104(g), reads as follows:

> Business Enterprises. The City shall not engage in any *purely commercial or industrial enterprise*, except upon a majority vote of the voters of the City voting on the question, unless the enterprise was engaged in by the City at the time the Charter becomes effective, or unless engaging in the enterprise is elsewhere specifically authorized in the Charter. (Emphasis added.)

Because City Charter section 104(g) contains a prohibition against establishing "any purely commercial or industrial enterprise, except upon a majority vote of the voters" and because the CLA concluded that a public bank's "services are purely commercial and governed by commercial banking law . . . a public bank would be considered 'purely commercial' and would require voter approval." (CLA's Report dated 2/27/20, at p. 5.) However, as set forth in AB 857, a public bank's functions and services are not "purely commercial." Moreover, a public bank is not governed solely by commercial banking law (as found in the California Finance Code and its associated regulations) as the CLA suggests, but rather is governed by a statutory scheme that includes provisions found in the Corporations Code, Government Code, and Revenue and Taxation Code -- which transcend traditional commercial banking regulations.

As a preliminary matter, the term "commercial enterprise" is not expressly defined in the City Charter. However, the plain meaning of the word "commercial" is defined as "involving or

relating to the buying and selling of goods;" while the word "enterprise" means "a company or business, often a small one." (*See* Collins Cobuild Advanced Dictionary *Commercial* and *Enterprise* at https://www.collinsdictionary.com/us/dictionary/english/commercial-enterprise (2020).) Webster's Dictionary further defines "commercial" to mean "viewed with regard to profit." (*Commercial* at https://www.merriam-webster.com/dictionary/commercial (2020).) Thus, even if for the sake of argument, a public bank in the City is engaged in "commercial" activities, i.e., the "buying and selling of goods" (e.g., financial services) for "profit," it should be pointed out that the term "commercial enterprise" is also modified in City Charter section 104(g) by the word "purely." Therefore, the City Charter more accurately limits the City from engaging in any activity to form a company or business that is "purely," i.e., solely engaged, in the buying and selling of such goods for profit without prior voter approval. Yet, the CLA's analysis essentially dismissed the importance of the qualifying term "purely," even though it appears in Section 104(g).

In fact, the CLA's view that a public bank would be a "purely commercial . . . enterprise," was rejected by the Legislature when it stated:

> It is the intent of the Legislature that this act authorize the lending of public credit to public banks and authorize public ownership of public banks ***for the purpose of achieving cost savings, strengthening local economies, supporting community development, and addressing infrastructure and housing needs for localities.*** (AB-857 Section 1 (emphasis added).)

Here, the Legislature does not provide for public banks to be formed so that they can engage in "purely commercial" banking activities; rather, a public bank's functions include many non-commercial aspects, including performing functions that serve the public interest, such as "achieving cost savings, strengthening local economies, supporting community development, and addressing infrastructure and housing needs for localities." In addition, AB 857 prohibits a public bank from even competing with commercial banks. (*See* Cal. Gov't Code 57604(b) & (c).) In essence, a public bank's functions include the achievement of public policy objectives, unlike the setting up of a "purely commercial enterprise" which would compete with commercial banks.

The conclusion that a City public bank would not be a "purely commercial enterprise" is further supported by the fact that AB 857 requires that prior to submitting an application to organize and establish a public bank with state regulators, the City must conduct a study to be submitted to the state that includes "[a] discussion of the purposes of the bank including, but not limited to, achieving cost savings, strengthening local economies, supporting community economic development, and addressing infrastructure and housing needs." (Cal. Gov't Code §§ 57606(a), (c).) In addition, the study may include "[a] fiscal analysis of benefits associated with starting the proposed public bank, including, but not limited to, cost savings, jobs created, jobs retained, economic activity generated, . . . private capital leveraged . . . [a] qualitative assessment of social or environmental benefits of the proposed public bank . . . ." (Cal. Gov't Code §§ 57606(b), (c).) The inclusion of these "non-commercial" considerations also shows that a public bank is not

solely engaged commercial activities but rather is also engaged in securing benefits for the public.

In addition, the notion that a public bank is a "purely commercial enterprise" runs counter to the fact that AB 857 requires that public banks be formed as nonprofit corporations. (*See* Cal. Corp. Code §§ 5130, 7130; Fin. Code § 1004; Gov't Code §§ 57600(b), 57601; Cal. Rev. & Tax. Code § 23701aa.) Thus, while a nonprofit public bank's functions include engaging in "commercial banking business or industrial banking business," it will not be driven by a "pure" commercial profit motivation.

The analysis above shows that the CLA's conclusion that a motion to submit a public bank application must be first approved by the voters on the basis that a public bank's services "are purely commercial and governed by commercial banking law" is incorrect. Rather, a City public bank would not only be engaged in the provision of commercial or industrial banking services regulated by the Finance Code, but would also engage in various non-commercial activities that go beyond those delineated by commercial bank regulations. The City Charter prohibition against engaging in "any purely commercial or industrial enterprise, except upon a majority vote of the voters," is similar to the prohibition against the use of public resources and funds without a public purpose, a rule with which general law cities must comply. (*See* Cal. Const. art. XVI, § 6.) Since charter cities may avoid this rule, it makes sense that the City adopted City Charter Section 104(g) to impose a safeguard (i.e., voter approval) as a check against the City engaging in "purely" for-profit commercial activities without a clear public purpose. However, the voter approval safeguard is unnecessary here since a public bank would not be a "purely commercial enterprise." And, in the absence of caselaw construing City Charter section 104(g), it is very likely that a court will defer to the City Council's own reasonable findings to this effect.

IV. *AB 857 Expressly Permits the City Treasurer to Deposit City Funds in a Public Bank*

The CLA's Report correctly notes that the City Charter designates the City Treasurer as the custodian of all money deposited into the City treasury and that state law provides that the Treasurer is responsible for safekeeping these monies and selects depositories that "in his or her judgment is to the public advantage." (*See* City Charter § 301; Cal. Gov't Code §§ 53649; 53682.) However, in addressing the issue of whether the Treasurer can make deposits in a City established public bank, the CLA incorrectly states that "[a]ny change to the Treasurer's fiduciary authority or depository options would require a Charter Amendment in addition to potential changes in State law." (CLA's Report dated 2/27/20, at p. 6.)

The City Charter provides, "[t]he Treasurer shall perform those duties imposed upon City treasurers by any law of the state applicable to the City . . . ." (L.A. City Charter § 301(g).) As adopted, AB 857 amends and adds to the "law of the state" to delineate the parameters of public banking, including the role of city treasurers in the process. Government Code section 53635.2, as amended, provides that all money under the custodianship of the Treasurer shall be deposited in "state or national banks, public banks . . . ." Thus, deposits into a public bank are expressly allowed. And, Government Code section 57603, as amended, permits the City Treasurer to

invest in public bank-issued debt. Since City Charter section 303 specifies that "[t]he Treasurer may deposit the money held in the Treasury in the institutions and upon terms provided by law," viewed alongside of AB 857's provisions, there should be no doubt that the City Treasurer is expressly permitted to deposit funds in a public bank.

V. *Recommendations*

Currently, the City utilizes the services of several banks, each serving particular services and functions, and spreading the risk among its banking partnerships. AB 857 provides a clear process whereby a public bank can be established and added to the City's financial system to accomplish objectives that public banks may be better equipped to serve. Based on the analysis above, the City may apply to establish a public bank with state regulators without having to first go through a voter approval process or enacting a City Charter amendment. In order to facilitate those efforts, the Chief Administrative Officer should be tasked by the City with outlining and supervising a path to establish a public bank as expeditiously as possible pursuant to AB 857, with the goal of putting forth a viable plan by December 31, 2020.

We are available to address any additional questions you may have regarding this important public policy issue.