

Approved: 2-18-2011

Date

## MINUTES OF THE HOUSE FINANCIAL INSTITUTIONS COMMITTEE

The meeting was called to order by Chairman Forrest Knox at 3:30 p.m. on February 17, 2011, in Room 152-S of the Capitol.

All members were present except Representatives Hermanson and O'Hara, both of whom were excused.

### Committee staff present:

David Wiese, Office of the Revisor of Statutes  
Melissa Calderwood, Kansas Legislative Research Department  
Cindy Lash, Kansas Legislative Research Department  
Gary Deeter, Committee Secretary

### Conferees appearing before the Committee:

Katrin Osterhaus, Auditor, Legislative Post Audit

### Others attending:

See attached list.

The Chair welcomed Katrin Osterhaus, Legislative Post Audit, who briefed the committee on a 2008 audit assessing possible efficiencies to be gained by merging the Kansas Office of the Bank Commissioner, the Kansas Department of Credit Unions, and the Kansas Securities Commissioner (Attachment 1). After giving the background of each agency, she summarized the findings of the study:

- Many states organize financial regulatory functions under a single agency.
- The three Kansas financial regulatory agencies could save at least \$555,000 through consolidation and other efficiency measures.
- If the agencies are consolidated, differing administrative, philosophical, and fee structures would need to be addressed and synthesized. (A chart on page 4 illustrates the varying complexity of each agency.)
- Even if the agencies are not consolidated, a total of \$295,000 or more could be saved annually by instituting more efficient operations within each agency.

Ms. Osterhaus briefly commented on each finding and then fielded questions from committee members. Items:

- The study did not consider the impact of the federal Dodd-Frank Act, since the study was done in 2008.
- The study did not distinguish between a nationally chartered or state-chartered bank.
- Other than introducing a bill that died in committee, the legislature took no action on the study.
- Kansas is one of only five states with three or more agencies that regulate financial institutions.

The meeting was adjourned at 4:00 p.m. No further meeting was scheduled.

## HOUSE FINANCIAL INSTITUTIONS COMMITTEE GUEST LIST

DATE: FEBRUARY 17 2011

[illegible]



LEGISLATURE OF KANSAS

## LEGISLATIVE DIVISION OF POST AUDIT

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September 11, 2008

To: Members, Legislative Post Audit Committee

Senator Derek Schmidt, Chair  
Senator Les Donovan  
Senator Anthony Hensley  
Senator Nick Jordan  
Senator Chris Steineger

Representative Virgil Peck Jr., Vice-Chair  
Representative Tom Burroughs  
Representative John Grange  
Representative Peggy Mast  
Representative Tom Sawyer

This report contains the findings, conclusions, and recommendations from our completed performance audit, *Financial Regulatory Agencies in Kansas: A K-GOAL Audit Determining Whether Functions Could Be Combined to Gain Cost Efficiencies*.

The report also contains appendices showing the various federal regulators and national associations, the financial regulatory agencies in each state, and the assumptions and methodologies used to estimate the cost savings reported in the audit.

This report includes several recommendations for the Legislature, Office of the Bank Commissioner, Department of Credit Unions, and for the Office of the Securities Commissioner. We would be happy to discuss these recommendations or any other items in the report with any legislative committees, individual legislators, or other State officials.

Barbara J. Hinton  
Legislative Post Auditor

Attachment 1  
House Financial Institutions Committee  
Date 2-17-11

## Get the Big Picture

Read the sections and features:

1. **Executive Summary** - an overview of the questions we asked and the answers we found.
2. **Conclusion and Recommendations** - appear in boxes at the end of the report sections. They also are referenced in the Executive Summary.
3. **Agency Response** - is included as the last Appendix in the report.

## *Helpful tools for Getting to the Detail*

- In many cases, an “At a Glance” description of the agency or program appears within the first few pages of the main report.
- **Side Headings** point out key issues and findings.
- **Charts and Tables** found throughout the report help tell the story of what we found.
- **Narrative text boxes** can highlight interesting information, or provide detailed examples.
- Appendices include additional supporting detail, along with the **Scope Statement and Agency Response(s)**.

## EXECUTIVE SUMMARY

LEGISLATIVE DIVISION OF POST AUDIT

### Overview of Kansas' Financial Regulatory Agencies

**Three agencies regulate banks and trusts, consumer and mortgage lending entities, credit unions, and the securities industry in Kansas.** ..... page 3  
*All three agencies share similar missions to safeguard assets and investments and to protect customers through similar regulatory functions such as conducting routine exams, investigating fraud, and taking enforcement actions. During fiscal year 2007, the three agencies combined spent about \$11.9 million on their regulatory activities. All three agencies are entirely fee-funded, and some of the excess revenues are transferred to the State General Fund.*

**Over time, financial regulatory agencies in Kansas have undergone several structural changes.** ..... page 6  
*Since the late 1800s, financial regulation in Kansas has evolved and undergone a series of changes in the way its financial regulatory agencies have been structured. At various times, the regulatory functions of one agency have been part of other agencies, and then split apart. For example, the regulation of credit unions was performed through the Office of the Bank Commissioner in 1929, but was moved into a newly created Department of Credit Unions in 1968. The latest change involved moving the responsibilities of the stand-alone Office of the Consumer Credit Commissioner into a division in the Office of the Bank Commissioner in 1999.*

### **Question 1: Could the Department of Credit Unions, the Office of the Bank Commissioner, and the Office of the Securities Commissioner Be Combined To Achieve Operating Efficiencies and Reduce Costs?**

**Many states organize financial regulatory functions under a single agency.** ..... page 9  
*Several federal reports have noted that consolidation of financial regulatory agencies could enhance efficiency and produce cost savings, and could result in a more comprehensive regulatory approach. Kansas is one of only five states that have three or more separate agencies overseeing banks, credit unions, consumer mortgage lenders, and securities.*

*Banks and credit unions are regulated by a single agency in 43 states. Securities regulation is housed in the same agency that regulates banks and credit unions in 21 states and the District of Columbia. In 29 states, securities regulation is housed separately from bank and credit union regulators. Often securities regulation is housed within the Secretary of State's Office or the Attorney General's Office; in 6 states, it is housed in a separate stand-alone agency.*

**In Kansas, the three financial regulatory agencies could save at least \$555,000 a year through consolidation and other efficiency efforts.** *Of this amount, we estimated that at least \$260,000 in savings could be achieved through consolidation, and about \$295,000 could be saved through other operational efficiencies. Our estimates are conservative; they could be higher if the head of a consolidated agency explored other savings possibilities. We didn't include any one-time moving or training costs related to combining these agencies into a single office, but we think these one-time costs would be quickly offset by the annual cost savings we identified.*

.....page 12

**Consolidating the three agencies could save at least \$260,000 a year in salaries, benefits, and other operating costs.** *Most of the savings our model would generate come from eliminating or restructuring staff positions that would no longer be needed. For example, based on a review of other states' structures, our model assumes that a consolidated agency could operate with a single agency head and deputy director – which would result in the elimination of one agency head position and the associated salary and benefits. Other significant cost savings come from reducing the number of supervisory positions in the legal and registration functions of a consolidated agency.*

.....page 14

*Incidental cost savings associated with a combined agency would total about \$10,000 annually. Cross-training bank and credit union examiners could provide additional savings, but those savings are difficult to quantify and appear limited in the short run. However, we think the larger payout likely would come through more efficient scheduling and use of staff over time.*

**If the agencies are combined, several issues regarding how they are governed and operated will need to be addressed.** *For example, a decision would need to be made about whether a board is needed, and how it would be structured. Also, consolidating agencies could result in several challenges, such as balancing the differing philosophies of the individual agencies, and establishing appropriate accounting procedures to ensure that the fees generated by one industry don't subsidize another.*

.....page 20

**At least \$295,000 could be saved annually by making existing agency operations more efficient.** *Conducting credit union examinations only as often as required by law or as needed for problem entities could eliminate the need for two examiners and generate an estimated \$107,000 in annual savings. Additional savings could be achieved by eliminating routine trips to credit union branch locations, but we couldn't quantify the savings.*

.....page 22

*Having examiners at the Office of the Bank Commissioner work from home – as credit union examiners and inspectors in other agencies currently do – could save an estimated \$106,000. Also, the agencies could save at least \$80,000 a year by adhering to the space standards*

1-4

recommended by the Department of Administration. Finally, for a small sample of staff, we identified about \$2,700 in travel expenditures that didn't comply with travel reimbursement regulations or that didn't appear necessary.

**During our work we also found that a few banks and trusts weren't examined as often as required.** *State and federal law requires these entities to be examined every 18 months, and State and federal examiners alternate examinations to accomplish that. In reviewing the most recently completed examination cycles for the almost 300 entities examined, we noted that 4 exam cycles were more than 20 months apart; in three of those cases, the delays occurred because the federal exams didn't start on time.* ..... page 26

<b>Conclusion</b>	..... page 27
<b>Recommendations for legislative action</b>	..... page 28
<b>Recommendations for executive action</b>	..... page 28
<b>Appendix A: Scope Statement</b>	..... page 31
<b>Appendix B: Summary of Federal Regulators and National Associations in the Financial Industry</b>	..... page 32
<b>Appendix C: List of Financial Regulatory Agencies In All States and the District of Columbia</b>	..... page 35
<b>Appendix D: Assumptions and Methodologies</b>	..... page 40
<b>Appendix E: Agency Responses</b>	..... page 43

This audit was conducted by Katrin Osterhaus, Nathan Ensiz, Brad Hoff, and Justin Stowe. Leo Hafner was the audit manager. If you need any additional information about the audit's findings, please contact Katrin Osterhaus at the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612. You also may call us at (785) 296-3792, or contact us via the Internet at LPA@lpa.state.ks.us.

# Financial Regulatory Agencies in Kansas: A K-GOAL Audit

## Determining Whether Functions Could Be Combined To Gain Cost Efficiencies

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The Kansas Governmental Operations Accountability Law (K-GOAL) subjects any State agency or program to audits, reviews, and evaluations as determined by the Legislative Post Audit Committee. Through this process, the Legislature can, in the words of the Act, “retain and maintain appropriate and effective governmental operations, remediate defective governmental operations, and terminate inappropriate or obsolete governmental operations.”

The Committee is required to direct at least four audits each year under the law; it has chosen to focus these audits on efficiency and cost savings issues. The law states that each audit may determine whether the agency is still needed, whether another agency could effectively perform the functions of the agency or program, whether the agency or program could be operated more efficiently and still fulfill its intended purpose, and other factors as determined by the Legislative Post Audit Committee. The Committee has designated this audit of the financial regulatory agencies as the first audit under this revised K-GOAL focus.

Recently, legislators have expressed concerns that Kansas is one of few states that has separate agencies regulating financial institutions. Many states have a single agency responsible for regulating banks, credit unions, savings and loan associations, securities dealers, mortgage brokers, and the like. Legislators would like to know whether combining financial regulatory agencies in Kansas would achieve greater operational efficiencies and cost savings.

This performance audit answers the following question:

- 1. Could the Department of Credit Unions, the Office of the Bank Commissioner, and the Office of the Securities Commissioner be combined to achieve operating efficiencies and reduce costs?**

To answer this question, we gathered information about the agencies that regulate banks, credit unions, and securities in all 50 states. For a sample of states that have all three functions combined into a single agency, we gathered information about how they were organized, how many staff they had, and how many entities they regulate or examine. We gathered similar information about the three financial regulatory agencies in Kansas, and compared it to the states with a single agency.



Based on other states' structures, we developed a model for what might work in Kansas, including staffing levels, and computed how much the new model might reduce costs.

Finally, we analyzed exam cycles for the Department of Credit Union and the Office of the Bank Commissioner, looked at travel voucher records for a sample of staff at all three agencies, and reviewed other agency functions to determine whether other efficiencies could be achieved regardless of whether the agencies were combined.

A copy of the scope statement for this audit approved by the Legislative Post Audit Committee is included in *Appendix A*.

We conducted this performance audit in accordance with generally accepted government auditing standards, with certain exceptions.

We didn't test the time sheet data the Office of the Bank Commissioner and the Department of Credit Unions provided. That information was used to determine the amount of time employees spent conducting exams, traveling, and performing other work-related functions. In addition, the data used throughout the audit from other states are self-reported, and there was no way for us to assess the accuracy of that information. Regardless, these data are all that's available. We have no reason to believe that any of these data are so grossly or systematically wrong as to affect our findings.

The standards require that we plan and perform the audit to obtain sufficient and appropriate evidence to provide a reasonable basis for our findings and conclusions based on audit objectives. Except for the limitations described above, we followed these standards. Nevertheless, the savings presented throughout this report are based on a number of assumptions and estimates, and should be viewed with that in mind. The major assumptions we made are described in *Appendix D*.

Our findings begin on page 9, following a brief overview.

## Overview of Kansas' Financial Regulatory Agencies

### ***Three Agencies Regulate Banks and Trusts, Consumer and Mortgage Lending Entities, Credit Unions, and the Securities Industry In Kansas***

The Office of the Bank Commissioner, the Department of Credit Unions, and the Office of the Securities Commissioner all have similar missions to safeguard assets and investments and to protect customers. These agencies generally perform similar regulatory functions, including licensing and registering various financial entities, conducting routine exams, handling complaints, investigating fraud, and taking enforcement actions.

*Figure OV-1* summarizes these agencies' functions and staffing, as well as the types of entities they regulate.

Oversight occurs at both the State and federal levels. In addition, various national associations exist for these financial entities. Information about the federal entities and their roles is shown in *Appendix B*.

**During fiscal year 2007, the three agencies combined spent about \$11.9 million on their regulatory activities. *Figure OV-2* provides details on each agency's expenditures, and a combined total 5-year expenditure and staff-level history.**

**Some information about these agencies that the reader should be aware of:**

- **The three agencies are entirely fee-funded.** This means the money they collect from their respective industries must cover all their expenditures. In addition, by law each fee-funded agency also passes on 20% of the fees it secures—up to a maximum of \$200,000—to reimburse the State General Fund for accounting, legal, payroll, personnel, and other State governmental services.
- **Surplus revenues from the Office of the Securities Commissioner also are transferred into the State General Fund.** Since 1984, the Office has been required by law to transfer any end-of-year balance over a base amount from the Securities Fee Fund to the State General Fund. That base amount was \$500,000 until 1995, when it was reduced to \$50,000. That's because the Office's revenues from fees are much higher than their expenditures. In fiscal year 2007, the Office collected \$9.5 million in fees, but spent only \$2.5 million from the fee fund to run the agency. Consequently, about \$7 million in excess funds was transferred to the State General Fund. (The agency spent another \$1.1 million from its Investor Education Fund on agency operations, totaling the \$3.6 million expenditures shown in *Figure OV-2*).
- **In fiscal year 2006, a major State-chartered credit union switched to a federal charter.** The number of State-chartered credit unions has declined from 100 in fiscal year 2003 to 90 in fiscal year 2007. One of these credit unions was U.S. Central Credit Union, which changed its charter status from State to federal in fiscal year 2006. As a result, the National Credit Union Association became the oversight agency for this entity.

This change resulted in a \$36 billion drop in assets the Department of Credit Unions is responsible for examining, for a decrease of 92%. Overall, the Department's staffing has decreased by one examiner since that time period.

**Figure OV-1  
Mission and Functions of Credit Union, Bank, and Securities  
Financial Regulatory Agencies in Kansas**

	Office of the State Bank Commissioner	Department of Credit Unions	Office of the Securities Commissioner
Stated Mission	To ensure the integrity of regulated providers of financial services through responsible and proactive oversight, while protecting and educating consumers	To protect Kansas citizens and credit union members from undue risk through the examination and supervision of Kansas-chartered credit unions, and to ensure safe and sound operation and compliance with applicable laws and regulations	To protect and inform Kansas investors, to promote integrity and full disclosure in financial services, and to foster capital formation
Primary Statutory Functions	<ul style="list-style-type: none"><li>▶ examine State-chartered banks and trusts at least once every 18 months</li><li>▶ approve applications to incorporate new banks and mergers between banks</li><li>▶ register and examine consumer and mortgage lending entities</li></ul>	<ul style="list-style-type: none"><li>▶ examine State-chartered credit unions at least once every 18 months</li><li>▶ approve applications to incorporate new credit unions and mergers between credit unions</li></ul>	<ul style="list-style-type: none"><li>▶ license and examine securities professionals (Investment Advisors and Broker Dealers)</li><li>▶ register securities (e.g. stocks, mutual funds)</li><li>▶ investigate securities fraud and registration violations</li><li>▶ educate Kansas investors</li></ul>
Types and Numbers of Entities and Individuals Regulated (as of June 2008 or most recently available)	<ul style="list-style-type: none"><li>▶ 251 State-chartered banks</li><li>▶ 53 active State-chartered trust departments and companies</li><li>▶ 3,413 consumer and mortgage-lending companies, including pay-day loan companies, and mortgage lenders and brokers</li><li>▶ 2,758 loan originators</li></ul>	<ul style="list-style-type: none"><li>▶ 88 State-chartered credit unions</li></ul>	<ul style="list-style-type: none"><li>▶ 172 investment advisor firms</li><li>▶ 2,534 investment advisor representatives</li><li>▶ 1,662 broker dealer firms (a)</li><li>▶ 5,236 broker dealer agents (a)</li></ul>
Amount of Assets or Registered Securities Overseen (as of June 2008 or most recently available)	Banks: \$28.8 billion	\$3.7 billion	\$39.7 billion
	Trust Departments & Companies \$22.6 billion		
	Consumer and Mortgage \$439.7 billion (b)		
Amount of Loans or Registered Securities Overseen (as of June 2008 or most recently available)	Banks: \$19.5 billion	\$2.2 billion	
	Trust Departments & Companies N/A (c)		
	Consumer and Mortgage \$22.9 billion		
Current Board Structures	Nine-member board; monthly meetings	Seven-member advisory council; quarterly meetings	No board (informal council only)

(a) The Securities Commissioner's Office examined or investigated 43 broker dealer firms and agents and was in the process of examining or investigating 63 more by the end of fiscal year 2007, based mostly on complaints and to serve as a deterrent against fraud and abuse.

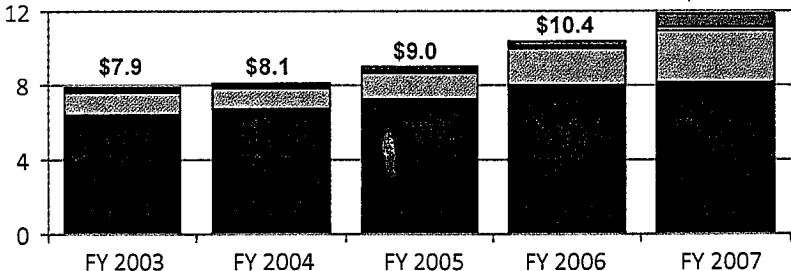
(b) Most of the consumer and mortgage lending entities operate nationwide. Consequently, the reported assets in this division reflect nationwide assets.

(c) Trust Department and Companies don't offer loans.

Source: The Division of Budget's 2009 Governor's Budget Report, and unaudited data provided by agency officials and staff.

- Combined operating expenditures for the three agencies increased by \$4 million from \$8 million to \$12 million, or nearly 50% from fiscal year 2004 to fiscal year 2007. A portion of this increase is due to extraordinary one-time expenditures in fiscal year 2007, such as a \$1 million investor education media campaign by the Office of the Securities Commissioner, and a \$545,000 computer upgrade at the Office of the Bank Commissioner.

**Figure OV-2**  
**Expenditures for the Office of the Bank Commissioner, the Department of Credit Unions,**  
**and the Office of the Securities Commissioner for Fiscal Year 2003 Through 2007**

Operating Expenses for Fiscal Year 2007								
Agency	Office of the State Bank Commissioner		Department of Credit Unions		Office of the Securities Commissioner		Total for All Agencies	
Type	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
Salaries & Wages	\$5,403,658	72.7%	\$685,639	81.6%	\$2,047,822	57.3%	\$8,137,119	68.7%
Contractual Services	\$1,254,745	16.9%	\$122,514	14.6%	\$1,431,200	40.0%	\$2,808,459	23.7%
Capital Outlay & Improvements	\$669,263	9.0%	\$17,657	2.1%	\$41,700	1.2%	\$728,620	6.1%
Commodities	<u>\$108,183</u>	<u>1.5%</u>	<u>\$14,395</u>	<u>1.7%</u>	<u>\$53,597</u>	<u>1.5%</u>	<u>\$176,175</u>	<u>1.5%</u>
Total Expense	\$7,435,849	100.0%	\$840,205	100.0%	\$3,574,319	100.0%	\$11,850,373	100.0%
FY07 Authorized Staff FTE	92.0		12.0		30.1		134.1	
Combined Operating Expense Totals for FY 2003-2007								
Combined Operating Expenses for all Three Agencies – Fiscal Years 2003 through 2007 (in millions)								
	<div><div></div> Capital Outlay</div> <div><div></div> Commodities</div> <div><div></div> Contractual Services</div> <div><div></div> Salaries and Wages</div>							
	FY 2003      FY 2004      FY 2005      FY 2006      FY 2007							
	Number of Authorized FTE Staff, FY 2003-2007							
	Banks	86.0	86.0	86.0	92.0	92.0		
Credit Unions	13.0	13.0	13.0	13.0	12.0			
Securities	<u>27.8</u>	<u>27.8</u>	<u>28.0</u>	<u>30.0</u>	<u>30.1</u>			
Total	126.8	126.8	127.0	135.0	134.1			

Source: LPA analysis of the Governor's Budget Reports, fiscal year 2005 to 2009.

In addition, salary expenditures have increased by almost \$1 million for the State Banking Commissioner, and by almost \$500,000 for the Office of the Securities Commissioner over that time period. The rise in salaries is mostly due to newly authorized positions within those two agencies. As *Figure OV-2* shows, for fiscal year 2006 the Legislature authorized six new positions for the Office of the Bank Commissioner and two new positions for the Office of the Securities Commissioner.

***Over Time, Financial  
Regulatory Agencies  
In Kansas Have  
Undergone Several  
Structural Changes***

Since the late 1800s, financial regulation in Kansas has evolved and undergone a series of changes. *Figure OV-3* summarizes the major changes that have occurred.

<b>Figure OV-3</b> <b>Brief History of Kansas' Financial Regulatory Agencies</b>	
Year	What Happened That Year
1891	The <u>Office of the State Bank Commissioner</u> was established.
1899	Savings and loan associations were placed under the Office of the Bank Commissioner's oversight.
1911	Kansas pioneered the Blue Sky laws by enacting the first Securities Act in the country, which required registration of securities and provided for prosecution of people who violated the Act. The function initially was housed in the Office of the Bank Commissioner and was later moved to the Kansas Corporation Commission.
1927	A <u>Savings and Loan Department</u> was established as a separate agency.
1929	Regulation of credit unions was placed under the Office of the Bank Commissioner's oversight.
1955	A separate <u>Consumer Credit Commissioner's</u> Office was established.
1968	A separate <u>Department of Credit Unions</u> was established.
1982	The <u>Office of the Kansas Securities Commissioner</u> was separated from the Kansas Corporation Commission.
1993	The Savings and Loan Department was abolished, and responsibility for savings and loans was placed under the Office of the Bank Commissioner.
1999	The Office of the Consumer Credit Commissioner was abolished and became the Consumer and Mortgage Lending Division, one of the two divisions within the Office of the Bank Commissioner.
Source: LPA analysis of previous LPA audit report (80-38) and information provided by agencies.	

In 1979, we conducted a sunset audit recommending that the functions of the State Bank Commissioner's Office, the Savings and Loan Department, the State Department of Credit Unions, and the Consumer Credit Commissioner's Office be consolidated under a single commissioner. The Legislature didn't act on this recommendation.

Most recently, the Office of the Consumer Credit Commissioner was moved into a division of the Office of the Bank Commissioner. This merger was the result of staffing issues within the Office of the Consumer Credit Commissioner. As the figure shows, at various times the regulatory functions have been merged under a single agency and then split apart again. For example, in 1929 regulation of credit unions was placed under the Bank Commissioner. Then in 1968, it was placed under a separate agency again.



**Question 1: Could the Department of Credit Unions, the Office of the Bank Commissioner, and the Office of the Securities Commissioner Be Combined To Achieve Operating Efficiencies and Reduce Costs?**

**ANSWER IN BRIEF:** *Kansas is one of only five states with three or more separate agencies that oversee financial entities and institutions. We estimated that at least \$555,000 could be saved annually by consolidating these agencies and implementing various cost-saving measures. Of that amount, about \$260,000 represents consolidation savings, most of which would be achieved by eliminating three staff and reducing the number of supervisors in the legal and registration functions. Cross-training credit union and bank examiners eventually could provide additional cost savings, but quantifying those savings will require a detailed analysis of the optimal location of examiners in relation to where the banks and credit unions are located. If the agencies are consolidated, several issues related to governance and operation would need to be addressed, including what type of oversight board would be needed.*

*We identified an additional \$295,000 in estimated annual cost savings from cost efficiencies that could be achieved regardless of whether the agencies are consolidated. These cost savings could be realized by reducing the number of credit union examinations to the minimum currently required by law, allowing bank examiners to work from home, following current travel regulations and by following space standards published by the Department of Administration. These and other findings are discussed in more detail in the sections that follow.*

***Many States Organize Financial Regulatory Functions Under a Single Agency***

In recent years, the U.S. Treasury Department and a research report issued by the Library of Congress have made a case for consolidating the nation's financial regulatory agencies. Arguments for consolidating include the following:

- **Differences between banks, credit unions, and other types of entities offering financial products and services to the public are becoming less pronounced.** For example, credit unions now offer services such as checking accounts, home mortgages, and commercial loans; services that used to be offered primarily by banks.
- **Consolidating financial regulatory agencies could result in enhanced efficiency and savings.** Efficiencies could result from combining common functions, which would reduce staffing levels and produce savings.
- **Consolidation could result in a more comprehensive regulatory approach.** A consolidated regulatory agency potentially could gain a clearer view of risks within the financial system as a whole than multiple regulatory agencies could.



However, these reports also mention several drawbacks related to consolidating multiple financial regulatory agencies. Those issues include placing more emphasis on one particular regulatory function over another (e.g. emphasizing examinations more than investigations), and equitably allocating resources received from the fees charged to the different groups of regulated institutions.

**Kansas is one of only five states that have three or more separate agencies overseeing banks, credit unions, consumer mortgage lenders, and securities.** Alabama, Oklahoma, South Carolina and Texas are the other four states. The remaining 45 states and the District of Columbia have either one or two agencies regulating entities providing financial services. More details are shown in *Figure 1-1*.

<b>Figure 1-1</b> <b>Summary of the Number of State Agencies Regulating Various Financial Entities and Institutions (a)</b>	
Number of Regulatory Agencies	Number of States and the District of Columbia
1 Agency	22 (b)
2 Agencies	24
3 or 4 Agencies	5
Total	51 (b)
(a) Includes oversight of banks, trusts, savings & loans, credit unions, consumer mortgage lending, and security entities. (b) Includes the District of Columbia. Source: LPA review of other states' financial regulatory agencies.	

In looking at the regulation of banks, credit unions, and securities in other states and the District of Columbia, we noted the following:

- **Banks and Credit Unions are regulated by a single agency in 43 states.** The other 8 states either regulate banks and credit unions through separate agencies or don't have state-chartered credit unions.
- **Securities regulation is housed in the same agency that regulates banks and credit unions in 21 states and the District of Columbia.** In 29 states, securities regulation is housed separately from bank and credit union regulators. Often securities regulation is housed within the Secretary of State's Office or the Attorney General's Office; in 6 states, it's housed in a stand-alone agency.

In most states, oversight over consumer mortgage lenders is part of the bank or securities agency. Only three states (Oklahoma, South Carolina, and Texas) have separate agencies to regulate those entities. *Appendix C* shows how all 50 states and the District of Columbia have structured their financial regulatory functions within their agencies.

**In 2004, Illinois Consolidated Four of Its Regulatory Agencies  
To Achieve an Estimated Cost Savings of \$9.4 Million**

In February of 2004, the Governor of Illinois merged the Office of Banks and Real Estate, Department of Financial and Credit Mortgage Lenders, the Department of Insurance, and the Department of Professional Regulation into a broad Department of Financial and Professional Regulation. The new agency has four divisions:

- **The Division of Banking** is responsible for the supervision, regulation, and examination of approximately 492 Illinois state-chartered commercial banks, about 200 trust departments or independent trust companies, and numerous foreign bank entities. In addition, the division supervises over 50 savings institutions, and over 1,800 mortgage bankers and brokers. Lastly, the division licenses almost 209 pawnshops.
- **The Division of Financial Institutions** is responsible for licensing and examining non-bank financial institutions that provide consumer loans, finance retail purchases, rent safe deposit boxes, exchange foreign currency, issue negotiable instruments, and provide financial planning and management services. It also regulates title insurance companies, state-chartered credit unions, and entities that offer check cashing, money order sales, and motor vehicle and title registration form processing.
- **The Division of Insurance** is responsible for regulating the insurance industry's market behavior and financial solvency, providing assistance and information, and fostering a competitive insurance marketplace.
- **The Division of Professional Regulation** licenses, registers, and examines over 1 million professionals from over 100 industries including architects, home inspectors, doctors, nurses, mental health professionals, boxers, and real estate professionals.

Illinois officials said the primary reasons for consolidation included eliminating duplicative functions, reviewing work schedules for productivity and accountability, and allowing functions such as human resources, payroll, and information technology to be combined.

In an audit conducted by the Auditor General of Illinois, the resulting savings from this consolidation were estimated at about \$9.4 million, as result of cutting 121 positions (of 946 total), and real property lease reductions.

In this audit, we were asked to explore the potential cost-savings and efficiencies from combining all three financial-regulatory agencies because of their similarities. However, the work performed within the Office of the Securities Commissioner does differ from the other two agencies in a variety of ways. For example, unlike the other agencies, the Securities Commissioner has law-enforcement staff to conduct criminal investigations.

**Enforcement Actions of the Division of Consumer and Mortgage Lending  
And the Office of the Securities Commissioner**

Neither the Office of the Securities Commissioner nor the Division of Consumer and Mortgage Lending within the Office of the Bank Commissioner have statutory requirements to perform exams within a certain time frame. Instead, they conduct examinations based on complaints they receive, as well as internal exam cycles for their regulated entities. Below is a summary of these agencies' results for the past three fiscal years.

<b>Office of the Kansas Bank Commissioner - Division of Consumer and Mortgage Lending</b>			
Type of Enforcement Action Taken	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008
Enforcement Actions Finalized	185	125	88
Fines and Settlements Collected	\$520,973	\$285,212	\$348,273
Cash Refunds to Consumers	\$2,332,834	\$1,654,674	\$3,095,405
<b>Office of the Securities Commissioner</b>			
Criminal Convictions	9	3	3
Administrative Orders	18	20	29
Fines Collected	\$34,844	\$2,276,778	\$49,427
Restitution/Rescissions	\$880,583	\$5,031,462	\$8,195,845

Source: Unaudited data provided by agency officials.

The Office also prosecutes its own cases when fraud is discovered. In addition, the types of examinations performed by the Office of the Securities Commissioner are substantially different from those conducted by the agencies that regulate banks and credit unions. Such differences may help explain why so many states haven't combined securities regulation with banks and credit unions.

Lastly, the reader should be aware that several of our analyses focused solely on the Division of Banks and not the Division of Consumer Mortgage Lending (CML). That's because, just like the Office of the Securities Commissioner, the Division of Consumer Mortgage Lending doesn't have statutory requirements on periodic examinations, and staff use a risk-based strategy to examine and investigate regulated entities. In addition, the entities being regulated, as well as how the work is performed, differs a lot across states, which made comparisons in this area not meaningful.

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***In Kansas, The Three  
Financial Regulatory  
Agencies Could Save At  
Least \$555,000 A Year  
Through Consolidation  
And Other Efficiency  
Efforts***

We estimated the cost of operating these agencies could be reduced by at least \$555,000, or about \$2.8 million over five years. Part of those savings would result from consolidating the three agencies. Other savings would come from enacting other operating efficiencies, which could happen whether or not the agencies were consolidated.

To develop our estimates, we had to make a number of assumptions related to staff workloads, travel patterns, and so on. *Appendix D* contains a list of the assumptions we made. When we needed to use expenditures from a previous year, we inflated the data to the current year. We tried to be as conservative as possible in our estimates so as not to overstate the potential savings.

We think that savings could be significantly higher in the future if the head of the consolidated agency initiated a detailed examination of the optimal location of examiners in relation to where the banks and credit unions are located, and adjusted the examination schedules accordingly.

In addition, a consolidated agency could realize further savings by increasing the use of automation and technology to reduce the amount and length of travel needed and to achieve other potential operating efficiencies.

Finally, it should be noted that, in estimating cost savings related to consolidation, we didn't compute any one-time moving or training costs related to combining these agencies into a single office. However, we think the annual cost savings we identified would quickly offset any one-time costs. *Figure 1-2* summarizes the estimated cost savings we identified.

The top portion of the figure shows our estimate of \$260,000 in annual savings that could be achieved through consolidation. The bottom part of the figure shows the estimated \$295,000 in potential savings that could come from having the agencies operate more efficiently—whether or not they are consolidated. These two categories of cost savings are discussed separately in the sections that follow.

**Figure 1-2**  
**Summary Table of Estimated Cost Savings**  
**(2007 and 2008 Fiscal Year Figures Inflated to Fiscal Year 2009)**

Actions That Could Produce Estimated Savings	Cost Savings				Offsetting Costs	Total Savings
	Salaries & Benefits	Rent	Travel	Other Incidental Savings		
Estimated Savings That Could Be Achieved Through Consolidation						
Eliminate 2 of 3 agency heads; Create 1 agency deputy	\$ 101,600	\$ 3,600	\$ -	\$ 1,100	\$ -	\$ 106,300
Eliminate 2 support positions	\$ 87,700	\$ 7,100	\$ -	\$ 800	\$ -	\$ 95,600
Restructure legal, registration, and examination positions	\$ 46,200	\$ -	\$ -	\$ -	\$ (2,400)	\$ 43,800
Economies of scale by sharing equipment, etc.	\$ -	\$ -	\$ -	\$ 10,400	\$ -	\$ 10,400
Cross-Train bank and credit union examiners	\$ 5,600	\$ -	\$ 4,000	\$ -	\$ (5,700)	\$ 3,900
Subtotals of Estimated Savings Achieved Through Consolidation	\$ 241,100	\$ 10,700	\$ 4,000	\$ 12,300	\$ (8,100)	\$ 260,000
Estimated Additional Savings That Could Be Achieved Through Operational Efficiencies (with or without consolidation)						
Examine credit unions only as often as required	\$ 83,800	\$ -	\$ 19,500	\$ 3,300	\$ -	\$ 106,600
Allow bank examiners to work from home	\$ -	\$ 147,500	\$ -	\$ -	\$ (41,400)	\$ 106,100
Reduce all agencies to rental space standards (a)	\$ -	\$ 80,200	\$ -	\$ -	\$ -	\$ 80,200
Require agencies to follow State travel regulations (b)	\$ -	\$ -	\$ 2,200	\$ -	\$ -	\$ 2,200
Eliminate inefficient trips (b)	\$ -	\$ -	\$ 500	\$ -	\$ -	\$ 500
Subtotals of Estimated Additional Savings Achieved Through Operational Efficiency	\$ 83,800	\$ 227,700	\$ 22,200	\$ 3,300	\$ (41,400)	\$ 295,600
Grand Total	\$ 324,900	\$ 238,400	\$ 26,200	\$ 15,600	\$ (49,500)	\$ 555,600

(a) This includes "monumental building surcharge" costs levied against agencies located in Shawnee county to fund operations of the State Capitol, the Judicial Center, and other buildings.

(b) The savings shown here are only partial savings that might be achieved. We identified these savings from reviewing fiscal year 2008 travel vouchers for a sample of three staff within each agency. The sample wasn't representative so it couldn't be projected agency wide; consequently, we didn't inflate these data. We think the savings would be greater here.

Source: LPA calculations using agency rental contracts, travel vouchers, compensation figures, and variable cost figures.

## SAVINGS ACHIEVED THROUGH AGENCY CONSOLIDATION

### ***Consolidating the Three Agencies Could Save At Least \$260,000 A Year In Compensation and Other Operating Costs***

As noted earlier, financial regulatory agencies could be combined in a number of ways. For the purposes of this audit, we assumed that all three agencies and their current staff of about 144 employees would be combined into one larger umbrella agency.

To estimate the savings that could result from consolidating these three agencies, we gathered basic information about them and compared it to similar information from four other states—Nebraska, Kentucky, Washington, and Wisconsin. We selected these states for our comparisons because they all have a single agency to regulate credit unions, banks, and securities, and they were similar to Kansas in terms of geographic size and the number of entities they regulate.

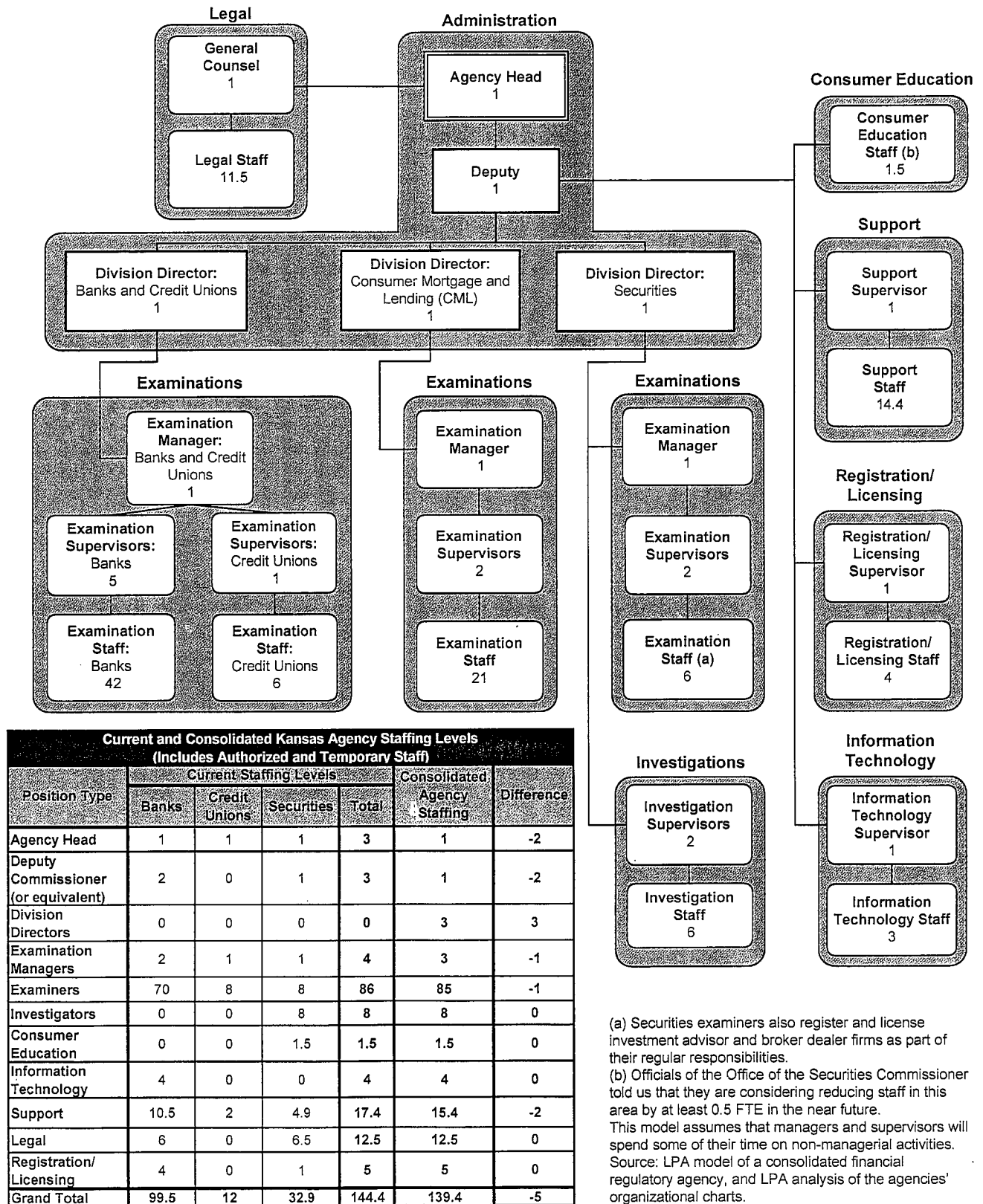
Based on the structures we saw in these states, we created an organizational model for what a consolidated financial-regulatory agency could look like in Kansas. That organizational model is shown in *Figure 1-3*.

As the figure shows, our consolidated-agency model would have a single agency head with three main divisions: Banks and Credit Unions, Consumer and Mortgage Lenders, and Securities. We combined the banks and credit union examiners under a single division because that was the most common organizational structure in the states with consolidated agencies. In addition, this division includes examinations of trusts. That's because bank examiners also conduct trust exams. In this model we assumed that, as in the past, some supervisory positions also perform non-supervisory duties.

**Most of the savings our model would generate come from eliminating or restructuring staff positions that would no longer be needed.** To help us in estimating the number of staff positions that might be needed under a consolidated-agency model, we grouped all staff into functional areas, such as administration, support, legal, and examinations. For each group, we computed and compared staffing ratios for the three Kansas agencies as they currently exist, and for our four comparison states. In addition, we reviewed the other states' organizational charts, and gathered and considered other relevant information. Based on these efforts, we identified the following potential for cost savings:

- **Cutting two agency head positions but creating one deputy commissioner would save about \$106,300 in salaries and benefits, rent, and other incidental costs annually.** Our review of the organizational charts of our four comparison states showed their agencies most commonly had an agency head, a deputy, and division leaders for various different functions. We structured our consolidated-agency model this way. That resulted in cutting the salaries and benefits (hereafter

**Figure 1-3**  
**LPA Model for an Agency Consolidation of the Department of Credit Unions,**  
**Office of the Bank Commissioner, and Office of the Securities Commissioner**

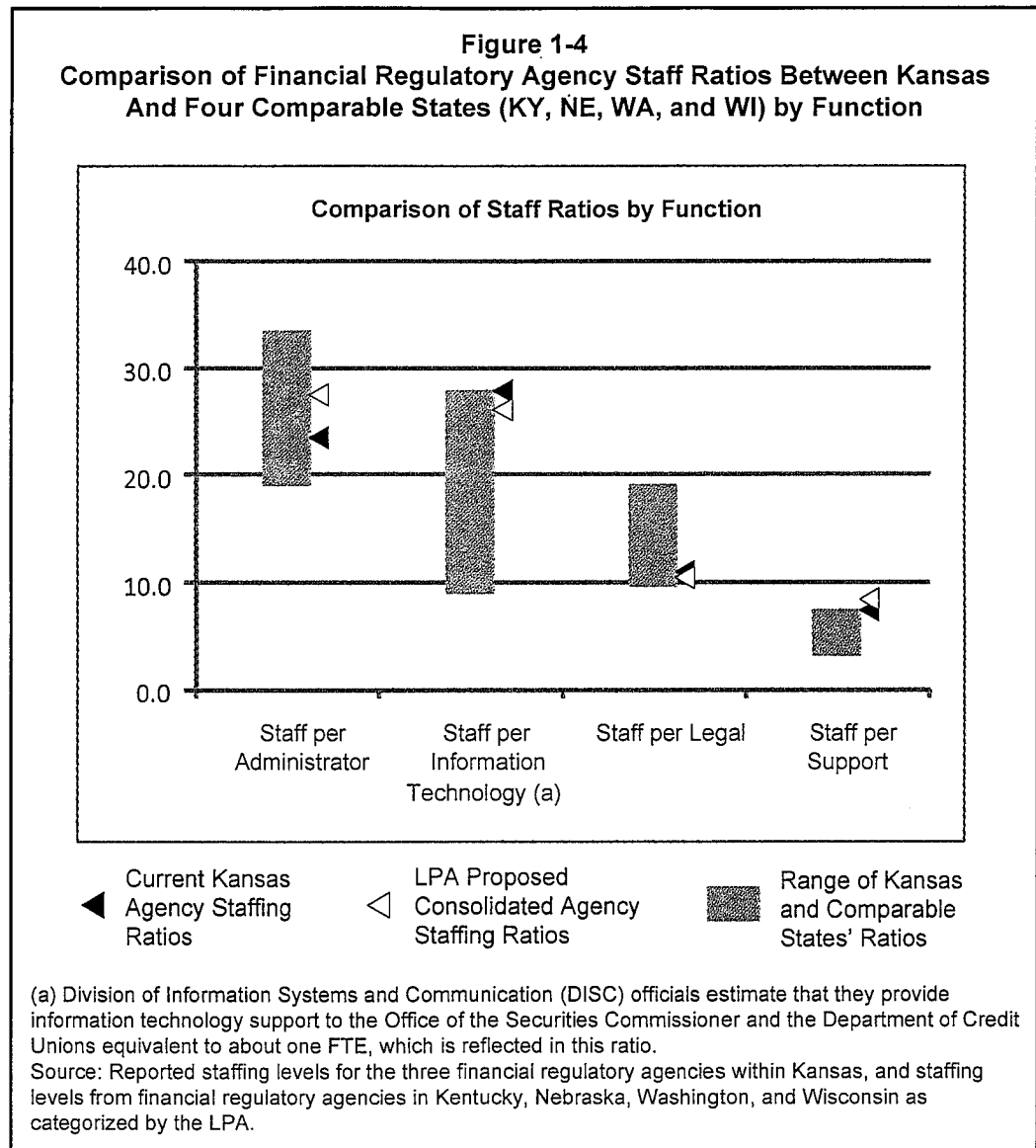


referred to as compensation) for two agency heads' compensation amounts and creating a new deputy position. The net savings—along with rent and incidental cost savings from one fewer position—resulted in \$106,300.

- **Cutting two support staff positions would save about \$95,600 in compensation, rent and other incidental costs annually.** Operating a larger consolidated agency can provide opportunities for greater economies of scale, especially in support areas such as purchasing and payroll functions, or tasks like answering the phone. To estimate the savings that might be achieved in the area of support, we computed the current ratios of support staff to total staff in each of the financial regulatory agencies in Kansas as they currently exist. Assuming that the consolidated agency could operate at least as efficiently as the Office of the Bank Commissioner, which had a ratio of one support staff for every 8.5 non-support staff positions, we calculated that a consolidated agency would need two fewer support staff, producing associated cost savings of about \$95,600 a year.
- **Converting two supervisory positions into non-supervisory positions, and reducing their compensation accordingly, would save about \$46,000.** For our consolidated-agency model we converted one of the two General Counsel positions and one of the two registration supervisor positions to non-supervisory positions, for a cost savings of about \$46,000. Even though Kansas appears to have more legal staff overall than 3 of our 4 comparison states, we didn't eliminate any of these positions entirely. That's because officials from the Office of the Securities Commissioner told us Kansas is one of a few states in the nation that has prosecution power and will try its own civil and criminal cases, which takes more legal staff. Officials from our comparison states told us that criminal cases generally are prosecuted through different offices, such as their Attorney General's Office. Currently, one staff at the Attorney General's Office spends about 10% of her time to provide legal advice to the Department of Credit Unions. We assumed this could continue under our model, or be absorbed by existing legal staff at the other agency.
- **About \$2,400 of the compensation cost savings would be offset by the need to equalize some positions' compensation levels.** Combining bank and credit union examiners under a single division and a single division head would require making the current credit union examination "manager" position equivalent to a bank examination "supervisor" position under the new structure. Bank exam supervisor positions currently make about \$2,400 a year more than the credit union manager position. To create parity, we equalized those compensation amounts and reduced our estimate of cost savings accordingly.
- **We made no changes to information technology staff.** Normally, savings in areas like information technology would be expected when several agencies are consolidated. However, in this case Kansas already had fewer information technology staff than the other states we looked at. The Office of the Bank Commissioner has four IT positions, and the Office of the Securities Commissioner and the Department of Credit Unions have no information technology staff. Instead, they receive technology assistance through about one FTE-equivalent staff person from the Division of Information Systems and Communications (DISC). Taking all these resources into account, the three agencies have about 1 information technology position for every 29 non-IT staff. In contrast, the four comparison states had a range of one IT staff member for every 9 to 17.8 non-IT staff members. Based on discussions we had with DISC officials

we assumed that the existing IT staff at the Bank Commissioner's Office would continue to serve the combined agency, with additional assistance from DISC as needed.

*Figure 1-4* shows how the current and proposed staffing ratios of Kansas compare to the upper and lower limits we found in our comparison states.



**Incidental cost savings associated with a combined agency would total about \$10,000 annually.** A larger, consolidated agency would be able to realize certain economies of scale because they likely wouldn't need as many duplicate copiers, printers, or other office equipment. To estimate potential savings in this area, we identified the types of expenditures that vary based on an agency's size and assumed those expenses could be reduced by 3%.



**Cross-training bank and credit union examiners could provide additional savings, but those savings are difficult to quantify.**

Examinations performed by bank and credit union examiners are essentially the same: they both conduct safety and soundness exams by reviewing the entities' capital, asset quality, business management, return on assets, and liquidity risk. The primary difference appears to relate to the size and complexity of the institutions and the transactions they examine—for example, credit unions are likely to have smaller loans for cars or home improvement, while banks are likely to have larger loans for such things as hotels or other commercial property.

In the course of this audit, we learned that Georgia cross-trained its credit union and bank examiners more than 10 years ago. Although officials there weren't able to quantify the cost savings related to cross-training, they said it gives them greater flexibility in scheduling examinations.

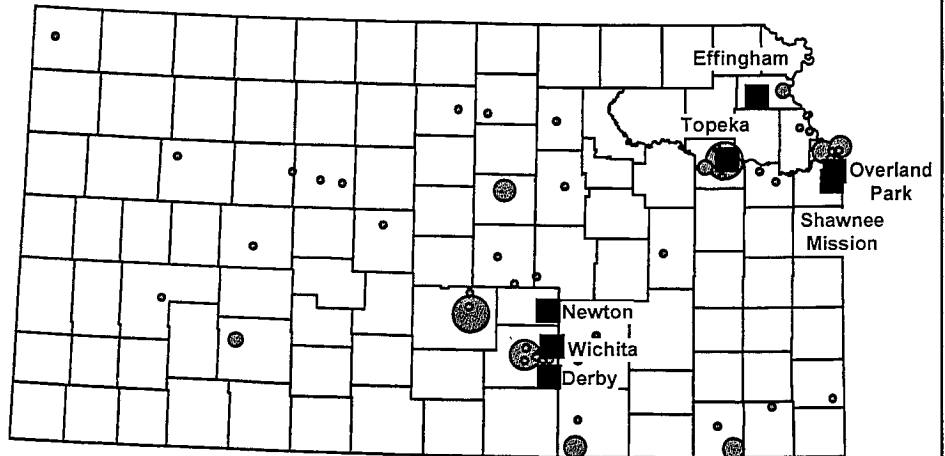
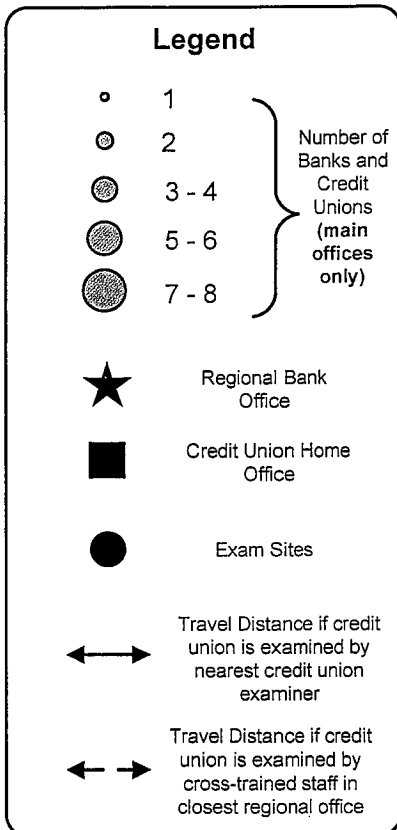
Currently, Kansas has 9 credit union examiners ( 7 full-time equivalent and 2 part-time staff) who work from their homes, and 48 bank examiners who work from 7 regional offices throughout the State. The maps in *Figure 1-5* show where these credit union and bank examiners are located in Kansas relative to the institutions they examine, and can help illustrate how greater flexibility in scheduling and conducting examinations could translate to cost savings.

As the top map shows, all the credit union examiners are located in the eastern part of the State and have to travel long distances to examine credit unions in western Kansas. The middle map shows that the Bank Commissioner has offices in Hays and Dodge City to examine the banks in western Kansas. If bank and credit union examiners were cross trained, both staff time and travel time and costs could be reduced.

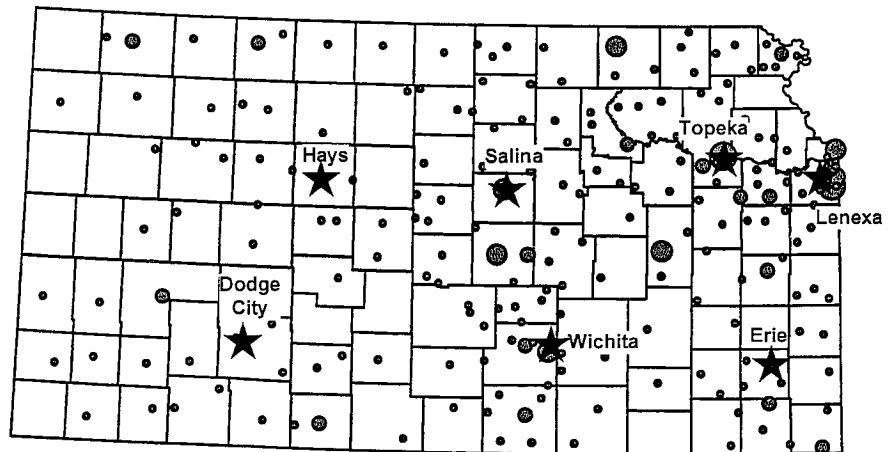
We noted that 26 credit unions were located closer to a regional Bank Commissioner's office than to a credit union examiner. If these credit unions were examined by cross-trained staff in the regional offices, the savings in travel costs would be an estimated \$4,000, and the savings in staff time would be about 220 staff hours, or an estimated \$5,600 in compensation. (See *Appendix D* for the assumptions we made in these calculations.) Because these savings would be partially offset by the need to spend about \$5,700 to equalize bank and credit union examiners' compensation, our total estimated savings in this area is about \$3,900 a year.

**Figure 1-5**  
**Examiner Locations of the Office of Bank Commissioner and Department of Credit Unions,**  
**and Main Office Locations of the Institutions These Agencies Regulate**

**Current Credit Union Examiner Locations and Credit Union Main Office Locations**



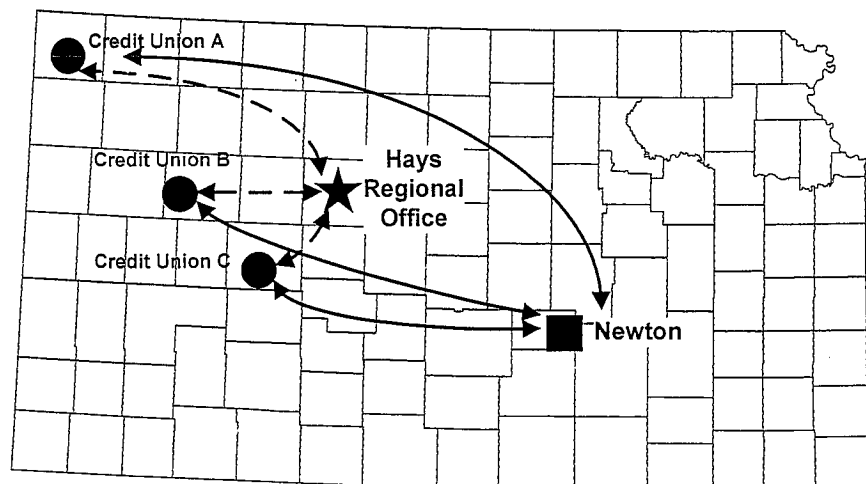
**Current Bank Examiner Office Locations and Bank Main Office Locations**



**Example of Travel Efficiencies Related to Cross-Training Bank and Credit Union Examination Staff**

We estimated the cost-savings that could be gained from the cross-trained examiners traveling from the office nearest the exam site, regardless of whether that office was a credit union examiners home office or a bank regional office.

As the example shows, travel to these three credit unions is much shorter from the regional bank office in Hays than from the nearest credit union examiner's home office in Newton.



Source: LPA analysis of data from Office of Bank Commissioner and Department of Credit Unions

Although the savings we've associated with cross-training may appear to be limited, the larger payout is likely to come through more efficient use of staff over the long term. With more than 390 financial institutions and 54 bank and credit union examiners, a cross-trained examination workforce would give agency management much greater flexibility in scheduling exam staff across these institutions. That increased flexibility could result in even lower travel costs, and could free up even more staff time, resulting in additional part-time or full-time positions being able to be eliminated.

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*If the Agencies Are Combined, Several Issues Regarding How They Are Governed and Operated Will Need To Be Addressed*

Through our discussions with agency officials in Kansas and other states and the literature we read, we identified several issues that would have to be considered before consolidating financial regulatory agencies. Each of these is discussed in the following sections.

**A decision would need to be made about whether a board is needed, and how it would be structured.** We reviewed the composition of boards attached to financial regulatory agencies for nine other states that have a single regulatory agency. As *Figure 1-6* shows, six of those states had no boards, two had multiple boards with about six members each, and one had a single 12-member board.

For comparison purposes, we also reviewed the board composition for three Kansas agencies that regulate multiple professions: the Boards of Healing Arts, Behavioral Sciences, and Technical Professions. These agencies' board membership ranges from 11 to 15, and members typically are composed of individuals representing the various professions being regulated.

**Consolidating agencies could result in several challenges, such as balancing the differing philosophies of the individual agencies.**

When we talked with officials in all three agencies about our consolidated-agency model, they raised the following concerns:

- **Differences in regulatory philosophies.** While the agencies included in this audit share a common mission of protecting the public, they accomplish this mission in different ways. The bank and credit union agencies are primarily concerned with assessing the overall financial safety, soundness, and solvency of the institutions they examine, whereas the Office of the Securities Commissioner focuses on the individual's right to purchase financial instruments that have merit and that have provided full disclosure. Agency officials shared concerns that a consolidated agency might not preserve their specific regulatory emphasis. Staff from other states, as well as the federal reports we reviewed, have echoed that concern.
- **Industry rivalries.** Another issue to acknowledge is the longstanding rivalry between banks and credit unions, which stems from competition for some of the same customers. The concern is that if the head of a consolidated agency came from either the banking industry or the credit union industry, the other industry may indirectly suffer.

**Figure 1-6**  
**Financial Regulatory Boards in a Sample of Other States**

State	Agency Name	Does Agency Have a Board?	Name (and Number) of Board Members	Board Type
Connecticut	Department of Banking	No	N/A	N/A
Florida	Office of Financial Regulation	No	N/A	N/A
Idaho	Department of Finance	No	N/A	N/A
Kentucky	Department of Financial Institutions	Yes	Financial Institutions Board (12)	Advisory
Louisiana	Office of Financial Institutions	No	N/A	N/A
Maine	Department of Professional and Financial Regulation	No	N/A	N/A
Nebraska	Department of Banking and Finance	No	N/A	N/A
Washington	Department of Financial Institutions	Yes	Division of Securities Advisory Committee (7)	Advisory
			Mortgage Broker Commission (7)	
			Escrow Commission (6)	
Wisconsin	Department of Financial Institutions	Yes	Banking Review Board (5)	Advisory
			Credit Union Review Board (5)	
			Savings Institutions Review Board (5)	
			Loan Originator Review Council (inactive)	

Source: LPA analysis of other states' financial regulatory agencies and interview with state officials.

- **Potential regulatory conflicts of interests.** For example, officials cited instances where securities broker-dealers are sometimes co-located with a bank. Even though the two are separate entities governed by different regulations, this creates sort of a symbiotic relationship in which each entity might benefit from the other's customers—customers of the securities dealer may decide to do their banking business with the bank and vice versa. Securities officials expressed concern that if the head of a consolidated regulatory agency came from the banking industry, in instances such as the one cited, there could be pressure not to enforce broker-dealer regulatory requirements as strictly, so as not to jeopardize the beneficial relationship with the bank.

Additionally, credit union and securities staff expressed concerns that preferential treatment would be given to the banking side when it comes to staff positions, other resources, or less-tangible decisions, such as the type of training approved. Similar trepidation was voiced by officials we spoke with in several of our comparison states.

- **A consolidated agency might be less responsive to Kansans.** Officials expressed concerns that a consolidated agency would result in more layers of bureaucracy, resulting in a lengthier decision-making process and possibly leading to consumer question or complaints not being addressed as quickly and efficiently as is currently possible. None of our comparison states have recently undergone consolidation.

**Appropriate accounting procedures would have to be established to ensure that the fees generated by one industry don't subsidize another.** Officials from all three Kansas agencies we talked to expressed concerns about how funding would be handled in a consolidated agency. Because all three agencies are fee-funded, the primary concern is that one industry would end up paying for the regulation of another; which could result in lawsuits against the State.

Officials from our comparison states also said that funding streams can present difficulties, but indicated they have found solutions. For example, Washington state recently revised its statutes and combined various fee funds into one operating fund. Officials told us they will still track expenditures separately to determine whether one industry subsidizes others over the long term. We also learned that in Illinois, the funding streams of the various regulated industries are kept separate and payments for services for the agency as a whole (e.g. information technology, payroll, etc.) are paid on a percentage-based allocation.

#### **COST SAVINGS ACHIEVED THROUGH OTHER OPERATIONAL EFFICIENCIES**

***At Least \$295,000  
Could Be Saved  
Annually By Making  
Agency Operations  
More Efficient***

As part of this audit, we also looked for efficiency measures that could be implemented to save costs regardless of whether the three agencies are consolidated. As *Figure 1-2* on page 13 showed, we identified at least \$295,000 in estimated savings, primarily by doing the following:

- examining credit unions only as frequently as required by law
- having bank examiners work from home—as credit unions examiners and several other audit and inspection-type staff do within the State
- reducing the amount of office space occupied by these agencies to conform to space standard guidelines established by the Department of Administration

The following sections talk about these and other items in more detail.

**Conducting credit union examinations only as often as required by law—or as needed for problem entities—could generate an estimated \$107,000 in annual savings.** State law requires banks and credit unions to be examined at least once every 18 months. The Division of Banking has adopted an 18-month examination cycle and actually alternates their examinations between State and federal examiners. However, the Kansas Department of Credit Unions examines all Kansas credit unions once every 12 months, creating the need for additional examination staff.

We checked to see whether the National Association of State Credit Union Supervisors (NASCUS) required states to inspect credit unions more frequently than every 18 months in order to be accredited. Officials there told us a 15-month cycle was viewed as a best practice, but it isn't required for accreditation.

If the Department were to adhere to the 18-month statutory examination cycle for non-problem credit unions, and continue to examine "problem" credit unions once every 12 months, only 65 of the 88 State-chartered credit unions need to be examined each year. Doing so would allow the Department to eliminate two full-time-equivalent examination positions, saving an estimated \$84,000 in compensation and \$23,000 in related travel costs and other incidental expenditures. This analysis continues to allow examiners to conduct all other associated monitoring visits for problem entities, as well as other activities they perform as part of their job duties.

**Additional savings could be achieved by eliminating routine trips to credit union branch locations, but we couldn't quantify the savings.** Credit union examiners in Kansas regularly visit all branch offices, based on the Department's internal policy to observe branch operations in person. In addition, they told us the loan files they pick for review often are located at a branch location. Neither the Division of Banking, nor any of our four comparison states' credit union examiners regularly visit all branch offices of the entities they regulate. Washington officials told us that, if a main credit union office is managed well, and no complaints exist, they assume the branch offices are managed similarly well. They also said their credit unions are automated in such a way that examiners can access their loans electronically from the main location.

We weren't in a position to say which credit union branch visits may have been necessary, so we couldn't estimate the cost savings that could result from reducing or eliminating these branch visits. However, doing so potentially could result in additional cost and staff time savings. For example, we identified 19 branch visits that three of the credit union examiners performed in fiscal year 2008.

One of those trips took an examiner from his home office in Shawnee to branch offices in Hays, Phillipsburg, and Quinter, costing \$630 in potentially unnecessary travel, food, and lodging costs, and taking four days of the examiner's time. Another one-day, 450-mile trip took an examiner from his home office in Derby to branch offices in Lincoln, Osborne and Mankato, as well as the main credit union in Beloit, costing \$210.

Even if the agencies aren't consolidated, savings could be achieved by re-locating one of the existing credit union examiner positions. As *Figure 1-5* showed, there aren't credit union examiners in the western part of the State to cover credit unions in that region, and examiners often have to travel long distances to the credit unions they examine out west. Re-locating the examiner position from Effingham—which has very few credit unions nearby—to a location further west, and restructuring the schedule for other examiner positions accordingly, potentially could reduce travel costs and staff travel time even further.

Having examiners at the Office of the Bank Commissioner work from home—as credit union examiners and others currently do—could save an estimated \$106,000. Examiners within the Office of the Bank Commissioner and the Department of Credit Unions spend most of their time on-site at the institutions they examine. Although credit union examiners in Kansas currently work out of their homes, 63 examiners of the Office of the Bank Commissioner work out of six

regional offices and the central administrative office in Topeka. *Figure 1-7* summarizes the estimated office rent that could be eliminated if these examiners worked from home.

There's precedent for having bank examiners work from home. Officials from Iowa told us their bank examiners have worked from home for over 40 years, and said the practice works well and saves money. Wisconsin officials also indicated their bank examiners are allowed to work from home. In Kansas, Department of Education auditors work from home when they aren't on-site at a school district. In addition, food and safety inspectors—who are being transferred from the Department of Health and Environment to the Department of Agriculture by the end of this September—will be required to work from home, eliminating the regional offices those staff previously worked from.

Officials from the Office of the Bank Commissioner told us bank examiners were allowed to work from home in the early 1980s, but regional offices were created because of legislative concerns related to the staff productivity and security of sensitive documents. Bank officials cited those same

<b>Figure 1-7</b> <b>Potential Savings from Allowing Bank and Consumer Mortgage Loan Examiners To Work from Home</b>		
Regional Bank Office	Number of Sq. Ft. Being Rented	Current Rental Cost
Dodge City	650	\$6,900
Erie	430	\$4,080
Hays	710	\$7,079
Lenexa	3,295	\$52,720
Salina	816	\$10,740
Wichita	2,100	\$34,545
Topeka (a)	2,200	\$31,394
<b>Total</b>	<b>10,201</b>	<b>\$147,458</b>
Offsetting costs (b)		-\$41,368
<b>Potential Savings from Allowing Bank Examiners To Work from Home</b>		<b>\$106,090</b>
(a) The Topeka bank office has 12,513 square feet. Because this space is occupied by 20 examiners and 36.5 other staff, we asked officials to allocate a reasonable portion of that office space to the examiner staff, which was 110 square feet per examiner. (b) Includes an allowance of \$50 a month for Internet accessibility for examiners who don't already have cell phones, as well as rental expenditures for one manager currently located in Wichita. Source: LPA analysis of lease agreement data.		

concerns in discussions with us. However, officials from Iowa told us they address productivity concerns through clear performance expectations and active management. In addition, the electronic transfer of confidential and sensitive records today is significantly different than 20 or 30 years ago, and safeguards can be put in place to ensure the secure storage and transfer of such records.

Bank officials also indicated that, although allowing examiners to work from home would save on rent expenses, it could increase some other costs. For example, they said, the Fair Labor Standards Act would require that examiners be paid from the time they left and returned to their homes, rather than from the time they arrived at and left the office. They said the same would be true when examiners had to meet at a central location to pick up team members before traveling to the exam site. However, because officials acknowledged that examiners typically live in the same city their regional offices are located in, we think those mileage costs could be minimal compared with the reduction in rent costs.

**The agencies could save at least \$80,000 a year by adhering to the space standards recommended by the Department of Administration.** The Department of Administration's office space standard for State agencies is an average of 210-250 square feet of usable space per person. That standard includes not only actual office space, but also hallways, break rooms, conference rooms, and the like. When agencies exceed those standards, the Department of Administration asks the agency to provide justification for the extra space. Rent is one of the major common expenses the three agencies incur. Combined, the three agencies will spend almost \$500,000 for office rent in fiscal year 2009, based on current lease agreements.

After taking into account the staff reductions mentioned earlier in this report, and assuming examiners in the Office of the Bank Commissioner could work from home, the combined agency would need office space for 70.4 full-time-equivalent staff in the Topeka and Wichita offices. If the leased space for those staff was kept at the Department of Administration standard of 250 square feet per employee, it would reduce current rent expenditures by slightly more than \$80,000.

**For a small sample of staff, we identified about \$2,700 in travel expenditures that didn't comply with travel reimbursement regulations or that didn't appear to be necessary.** When employees use their private vehicles for official State business, travel regulations require agencies to reimburse them at the lower of the State's private vehicle rate, or the State's rental car rate when rental



cars are available. We examined travel vouchers submitted by three field staff from each of the three agencies and found the following:

- In fiscal year 2008, the Department of Credit Unions and the Office of the Securities Commissioner paid about \$2,200 more than they should have paid in private-car reimbursements. Almost all these overpayments were made to two part-time credit union examiners who routinely use their private cars to travel to credit union examinations.
- We also identified about \$500 in credit union examiner travel expenditures that we thought weren't necessary. Those included travel reimbursements for an examiner to attend a legislative reception and a trip for an examiner to attend a ribbon cutting for a credit union.

Given our small sample size, we think it's possible that additional overpayments or unnecessary travel could exist.

## OTHER MISCELLANEOUS FINDINGS

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### *A Few Banks and Trusts Weren't Examined As Often As Required*

Federal law requires (small) insured banks and trusts to be examined every 18 months. K.S.A. 9-1701(a) mirrors that requirement and states that, "The commissioner or the commissioner's assistant or examiners shall visit each bank and trust company *at least once every 18 months*, ... for the purpose of making a full and careful examination ... of such bank or trust company...." [emphasis added].

Currently, State and federal bank examiners alternate examinations of individual banks and trusts every 18 months. In other words, State bank examiners are only required to review half the nearly 300 banks and trusts in Kansas every 18 months.

In reviewing the most recently completed examination cycles for these entities, we noted that, of the almost 300 bank and trust departments examined by either State or federal examiners, 13 bank and 5 trust examinations weren't done timely. The deviations from the required cycle generally weren't large: only four exam cycles were more than 20 months apart, and in three of those cases, the delays occurred because the federal examinations didn't start on time. Officials also told us that some delays occurred because the owner of the entity had died or because internal scheduling problems existed.

***Conclusion:***

Over the years, the Legislature has created a number of individual agencies to regulate certain professions or activities and protect Kansas citizens from potential harm. Although a few of those agencies have been eliminated or consolidated over time, most continue to exist as separate, stand-alone agencies. Many other states have gone much farther in consolidating regulatory agencies—either by broad mission or in total. Consolidating such agencies offers significant potential for them to reduce their operating costs and increase their administrative efficiencies.

Housing all the functions of the Credit Union Department and the Offices of the Bank Commissioner and Securities Commissioner within a single agency could result in reduced costs and greater efficiencies, and would more closely align agencies with similar broad missions. Because all three agencies are fee-funded, the savings that could be achieved could be used to increase automation and make other technological improvements, improve other areas of oversight and enforcement, reduce fees to the regulated industry, or the like.

Given the similarities that exist between the regulation of banks, trusts and credit unions, and given that most states regulate these entities under a single agency, we concluded that the Department of Credit Unions and the Office of the Bank Commissioner should be consolidated. Combining the regulation of securities with the other two agencies will achieve additional economies of scale, but the precedent for this organizational structure is not as clear cut. Although only six states have a stand-alone office for the securities commissioner, that office frequently is located within a secretary of state's office or an attorney general's office.

Finally, officials from the Office of the Securities Commissioner and the Department of Credit Unions have expressed concerns that their functions would be diluted if consolidation occurred, or that the services and protections they provide to the Kansans they serve might be diminished. These concerns should be fully aired in any legislative deliberations about the future organizational structure of the agencies. However, given how common it is in other states for these functions to be combined under a larger agency umbrella, we are certain that agency staff working together to achieve a common goal can find workable solutions to such obstacles.

***Recommendations for  
Legislative Action:***

1. To help achieve the goals of combining the three agencies with similar missions and functions, reducing operating costs, and increasing administrative efficiencies, the Legislature should consolidate the regulation of banks and credit unions under a single financial-regulatory agency. Currently, 43 states have combined these regulatory functions under a single agency.
2. The Legislature should consider consolidating the regulation of securities under that same financial-regulatory agency. This arrangement currently exists in 21 states and the District of Columbia. Because securities regulation in Kansas includes investigating and prosecuting securities violations, another consolidation option that could be considered would be placing the regulation of securities under the Attorney General's Office. Only six states have stand-alone agencies for regulating securities.
3. If a decision is made to consolidate the regulation of banks, credit unions, and securities under a single financial-regulatory agency, the Legislature will need to do the following:
  - a. establish qualifications for the executive director position for the new agency that take into account the broader nature of the entities the agency will be responsible for regulating.
  - b. establish a board structure for the new agency. Some states we reviewed have no board, some have boards for each major function being regulated, and one had a single combined board for the entire agency. Other Kansas agencies that regulate multiple professions have a combined board with representatives from all or many professions on that board.
  - c. establish a timetable for making the transition from three separate agencies to a consolidated financial-regulatory agency.
  - d. consider whether any statutory changes may be needed to ensure that the fees generated by one industry don't subsidize another.

***Recommendations for  
Executive Action:***

4. To help achieve significant operational efficiencies if these regulatory functions are consolidated under a single agency, the new agency management should cross train some or all of the bank and credit union examination staff to provide greater flexibility in scheduling exams. In addition, management should conduct a comprehensive review of the exam sites to be visited with a goal of reducing the overall distance individual examiners have to travel.
5. To help achieve significant operational efficiencies, whether or not a decision is made to consolidate regulatory functions under

a single agency, the Office of the Bank Commissioner should restructure its examination function so that regional offices could be closed and bank and consumer mortgage lending examiners could work from their homes. That practice would be consistent with the practices followed by auditors in the Department of Education, credit union examiners in the Credit Union Department, and food safety inspectors in the Department of Agriculture. Bank examiners in Iowa also have been working from home for 40 years.

6. To help achieve significant operational efficiencies, whether or not a decision is made to consolidate regulatory functions under a single agency, the Department of Credit Unions should do the following:
  - a. reduce the frequency of its examinations of credit unions with good CAMEL ratings to once every 18-months, as currently required by Kansas law. That requirement is the same as the requirement for Kansas banks.
  - b. revise its policy to visit branch offices only on an "as needed" basis.
  - c. eliminate unnecessary travel.
7. To ensure the Office of the Bank Commissioner complies with K.S.A. 9-1707, officials should ensure that bank and trust examinations are examined once every 18 months.
8. As office lease agreements expire for the three agencies, the agencies should compare the amount of square feet they have been renting to the Department of Administration's recommended space standards. If their square footage is higher, they should either make the necessary adjustments to meet the standard or seek an exemption from the Department of Administration.
9. The Department of Credit Unions and the Office of the Securities Commissioner should implement policies and procedures to ensure that they adhere to K.A.R. 1-18-1a, which calls for agencies to reimburse staff at the lesser of either rental car costs or private vehicle reimbursement rates.