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Testimony of the Department of Commerce and Consumer Affairs

**Before the
House Committee on Finance
Tuesday, February 25, 2020
12:30 p.m.
State Capitol, Conference Room 308**

**On the following measure:
H.B. 2628, H.D. 2, RELATING TO A BANK OF THE STATE OF HAWAII**

Chair Luke and Members of the Committee:

My name is Iris Ikeda, and I am the Commissioner of the Department of Commerce and Consumer Affairs' (Department) Division of Financial Institutions (DFI). The Department offers comments on this bill.

The purposes of this bill are to: (1) direct the Department to conduct a comprehensive review of relevant state laws to develop legislation to establish a state-operated bank of the State of Hawaii; and (2) appropriate funds to conduct the review.

The idea of a state bank worked in 1919 for North Dakota and in 2019 for American Samoa. In both North Dakota and American Samoa, the state bank and territorial bank, respectively, were established to meet the credit needs of the community. In North Dakota, farmers were unable to get loans for farm equipment or crops or animals from the few banks in the area. In American Samoa, the last U.S. bank was exiting the market, and the territory would be without a bank. The Department notes that both the state bank and the territorial bank do not have Federal

Deposit Insurance Corporation insurance. Deposits made in the state bank and in the territorial bank are backed by the full faith and credit of the state of North Dakota and the Territorial Government of American Samoa, respectively.

The State of Hawaii has established other funds when services were not available. For instance, the Hawaii Employers' Mutual Insurance Company was created to stabilize the market when insurers were exiting the workers' compensation area. The Hawaii Hurricane Relief Fund was created when private insurers stopped writing hurricane property insurance. For the financial sector, the Department does not believe there is a lack of credit available to consumers or businesses.

In 2012, the DFI issued a white paper entitled "Should Hawaii Establish a State Bank?".¹ The white paper considered various factors, including:

- (1) The Bank of North Dakota;
- (2) The Federal Reserve Bank of Massachusetts research report;
- (3) Access to credit by local businesses;
- (4) The lending capacity of local banks;
- (5) Stabilization of the state economy and finances;
- (6) Start-up costs; and
- (7) Public policy issues.

The DFI's white paper concluded that the State must first determine what a state-operated bank would accomplish and be used for before it can analyze the managerial factors, financial factors, and capital requirements involved in establishing this financial institution.

Thank you for the opportunity to testify on this bill.

¹ This white paper is available at: <http://cca.hawaii.gov/dfi/learn-more-banks/>.

DAVID Y. IGE
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EMPLOYEES' RETIREMENT SYSTEM
HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
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WRITTEN ONLY

TESTIMONY BY CRAIG K. HIRAI,
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON FINANCE
ON
HOUSE BILL NO. 2628, H.D. 2

**February 25, 2020
12:30 PM
Room 308**

RELATING TO A BANK OF THE STATE OF HAWAII

The Department of Budget and Finance opposes House Bill No. 2628, H.D. 2.

This subject was last proposed in the 2016 legislative session, and requires the Department of Commerce and Consumer Affairs (DCCA) to coordinate amongst eight other state agencies, to produce a comprehensive review of the State's laws relating to financial institutions, mortgage lending, housing development, agricultural development, and land use for the purpose of developing proposed legislation to establish a bank of the State of Hawaii.

The DCCA commissioner of financial institutions is required to submit status reports and a final report in 2022, which shall include a schedule of state funds to be transferred to the bank of the State of Hawaii from financial institutions that are serving as depositories for the State. Section 4 of the bill appropriates out of the compliance resolution fund, a to-be-determined sum for the fiscal year 2020-2021 for the purpose of conducting this review.

The Department questions the use of the compliance resolution special fund or the expenditure of any state funds for this purpose and opposes Section 3 of the bill to transfer all state funds into a yet-to-be-established bank of the State of Hawaii. One of the primary functions and responsibilities of the Department stated in the Hawaii Revised Statutes, is for the safekeeping, management, investment, and disbursement of funds deposited into the state treasury by all state departments. Regulated and insured commercial financial institutions utilized by the state have the capacity, experience, security and technology to carry out the banking needs of the state. Furthermore, keeping state funds at these financial institutions supports the local economy. Management of the state's funds ensures that cash is available when needed to cover the multitude of activities and programs at all the state's departments and the legislature.

Although the intent of the bill with respect to outcomes envisioned by creating a bank is not stated in the bill, establishment and operation of a State owned and operated bank would be a significant and expensive undertaking.

Thank you for the opportunity to submit testimony on this bill.

Presentation to The
Committee on Finance
February 2020, 12:30 P.M.
State Capitol, Conference Room 308

Testimony in Opposition to HB 2628, HD 2

TO: The Honorable Sylvia Luke, Chair
The Honorable Ty J.K. Cullen, Vice Chair
Members of the Committee

My name is Neal K. Okabayashi, the Executive Director of the Hawaii Bankers Association (HBA). HBA is the trade association representing eight Hawaii banks and two banks from the continent with branches in Hawaii.

HBA opposes the idea of establishing a state bank after a study made by various state departments and agencies.

Banks accept deposits, which are then used to write checks to obligors and make loans to borrowers with the ability repay the loans. Since the bill offers no guidance as to the function of the state bank, whether it is to accept deposits or make loans, or both, one must wonder what the purpose of this bill is.

Is A State Bank Needed?

There are eight Hawaii banks headquartered in Hawaii. There is no evidence that the Hawaii banks are unable to meet the depository or credit needs of our businesses and residents. In addition, there are already state agencies which do engage in lending activities to meet certain community needs.

Capital Costs

The capital necessary for a state bank to be adequately capitalized under FDIC regulations will depend on the risk-weighted assets of the state bank which will depend on its lending activity. The Federal Reserve Bank of Boston drafted a report, issued in 2011, which analyzed the costs of organizing a state bank in Massachusetts and concluded that the required capitalization would be \$3.6 billion which would be 21% of the state direct debt. Obviously, the capital required in Hawaii would be smaller but at the same time, no doubt the burden on the state finances will be large.

Startup Costs

The startup costs are likely to be significant especially if the state bank will engage in deposits and checks. The infrastructure and cybersecurity costs will be significant, as well compliance with a myriad of banking regulations, such as the Patriot Act which included amendments to the Bank Secrecy Act and an anti-money laundering act.

The bill provides for a withdrawal of state funds from banks. The Federal Reserve of Boston opined that if the state sought to withdraw funds from private depositories, it would be disruptive and would lead to a negative impact on the Massachusetts economy. Also, by impacting the Hawaii banks, there would be an adverse impact on Hawaii tax revenue as the franchise tax paid would be based on a lower revenue base.

This will also lead to a diminution of interest received by the state. Currently, the state funds are deposited to the winner of a public auction based on the interest rate the bank is willing to pay. Also, the state is protected from risk because the deposit is collateralized so the state does not have to rely on the limitations of FDIC deposit insurance.

If the state bank is going to engage in depository check writing activity or making payment to employees, then there may be a question whether it is eligible to use the Federal Reserve payment system or FedNow (a proposed Federal Reserve payment system in the planning stages) and will then have to rely on a limited private payment system.

The foregoing should be considered a part of the startup costs.

Bond Rating Impact

If the state is to rely on bonds as a source of funds, the state must assess the risk of a lowering of the bond rating.

Using State Funds

If the state bank will rely on state funds as a source of funds, that means other uses of state funds such as for operating expenses, payroll, rainy day fund, and other human services needs, will have to rely on a lower amount of funds for their needs.

Risk to State Funds

Hawaii banks are examined by both the federal and state examiners (unless you are a nationally chartered which banks are examined only by federal examiners) to determine if the bank is compliant with regulations and especially, if there is a safety and soundness issue which endangers the financial soundness of the bank.

The state bank and Hawaii will not enjoy the benefit of federal and state examiners assessing the state bank.

FDIC Cautions

The FDIC Division of Risk Management Supervision in December 2019 issued a supplement to their procedures manual on deposit insurance application. The supplement addressed applications for deposit insurance by non-community (niche or specialty banks), including public banks. The FDIC said that public banks are rare because “they present concerns regarding the institution’s ability to operate independently of the political process; a potential lack of continuity in the institution’s policies, management, and oversight which could result from change in the governmental entity’s leadership; and the institution’s ability to raise capital.” We should heed the caution of the FDIC.

Conclusion and Other Alternatives

It is crystal clear that a study is not needed because all other studies have shown the imprudence of a state bank. If the need is for credit, there are other alternatives within the state including through the Hawaii Finance and Development Corporation. The state can use existing loan programs and government agencies as a faster and more effective than establishing an entirely new state bank.

Thank you for the opportunity to submit this testimony in opposition to HB 2628, HD 2. Please let us know if we can provide further information.

Neal K. Okabayashi
(808) 524-5161



House Committee on Finance
Monday, February 25, 2020, 12:30pm
Hawaii State Capitol, Room 308

In Opposition to HB 2628 HD1, Relating to a Bank of the State of Hawaii

To: The Honorable Sylvia Luke, Chair
The Honorable Ty Cullen, Vice-Chair
Members of the Committee

My name is Stefanie Sakamoto, and I am testifying on behalf of the Hawaii Credit Union League, the local trade association for 51 Hawaii credit unions, representing over 800,000 credit union members across the state. We offer the following testimony in opposition to HB 2628, Relating to a Bank of the State of Hawaii.

HB 2628 HD2 requires a comprehensive review of financial institution law be conducted by several state agencies, and to explore the feasibility of a state-operated bank of the State of Hawaii.

Our main concern is simply that funds being deposited into a state bank would be insured by the state itself. Without the benefit of being insured by a separate entity like the National Credit Union Administration (which insures and oversees all credit unions in the State of Hawaii), the state would be in an extremely precarious situation in the event of any financial difficulty within the bank, and within the state.

Thank you for the opportunity to provide comments on this issue.



Environmental Caucus of The Democratic Party of Hawai'i

Tuesday, February 25, 2020

House Bill 2628, HD 2

Testifying in Strong Support

LATE

Aloha Chair Luke; Vice Chair Cullen; and Members of the Committee on Finance:

The Environmental Caucus of the Democratic Party of Hawaii stands in **STRONG SUPPORT** of HB 2628, HD 2. The purpose of this measure is to direct the Department of Commerce and Consumer Affairs to conduct a comprehensive review of relevant state laws to develop legislation to establish a state-operated bank of the State of Hawaii; and to appropriate funds to conduct the review.

In Hawai'i, there is a lot of public funds to consider. In 2016, the State of Hawai'i deposited more than \$4 billion (\$4,000,000,000) a year of public tax and bond revenue into private banks including over a billion dollars in Wall Street banks and \$3 billion in some of the local banks.

Here is an opportunity for Hawai'i to improve in the way that we are currently allowing only for-profit, private banks to make so many of the decisions regarding our public funds. Our values should call our Legislature to consider other models that may better serve the people of Hawai'i. Questions should be raised about where our public funds are being deposited, whether there is a fair rate of return on these public investments, and which bank should be entitled to profit from holding these public funds.

Current discussions around the creation of a state bank for Hawai'i are not new to this legislative session or during prior sessions. In fact, Native Hawaiian activists on Maui and O`ahu have been discussing the concept and benefits of a state bank since the 1980s as it is painful to watch our state struggle to make ends meet when there are ways we could be doing more to protect and build our assets.

There are many models of banking around the country and around the world that serve families and communities first instead of shareholders and lead successful economic development and asset building for the people and not just for corporate interests.

Take the Bank of North Dakota (BND) for example. It is a state-owned, state-run financial institution based in [Bismarck, North Dakota](#). It is the only government-owned general-service

bank in the United States. It provides its citizens services to promote the following: (a) economic development; (b) returns to the general fund; (c) partnering with local financial institutions; (d) role in disaster relief; (e) home ownership; (f) postsecondary education funding; and (g) infrastructure funding.

Here is another example in South Africa which is launching a new state-owned bank and investment fund. President Cyril Ramaphosa said in his 2020 State of the Nation Address on February 13, 2020, “The National Treasury and the SA Reserve Bank are working together to ease pressure on business and consumers. We have decided to establish a sovereign wealth fund as a means to preserve and grow the national endowment of our nation, giving practical meaning to the injunction that the people shall share in the country’s wealth. We are also proceeding with the establishment of a state bank as part of our effort to extend access to financial services to all South Africans.”

The SA Treasury added that the traditional rationale for introducing a state bank relates to addressing market failures, i.e., the state supplying services that privately-owned banks may be unable or unwilling to supply. Financial inclusion is often cited as the key reason for the establishment of state-owned retail banks.

The following is a list of State Banks:

- [Bank of North Dakota](#)
- [Bankwest](#) — the Bank of Western Australia, now owned by [Commonwealth Bank](#)
- [Kiwibank](#) (state-owned bank in New Zealand)
- [Puerto Rico Government Development Bank](#)
- [State Bank of India](#) (a once private commercial bank that was nationalised by the [Government of India](#))
- [State Bank of New South Wales](#) (now part of the [Commonwealth Bank](#))
- [State Bank of Pakistan](#) (The bank of [Pakistan](#) was inaugurated by the [Quaid-e-Azam](#) on 1 July 1948 at [Karachi](#))
- [State Bank of South Australia](#) (now the Bank of South Australia, owned by [St. George Bank](#))
- [State Bank of Victoria](#) (now part of the [Commonwealth Bank](#))
- [State Bank of Vietnam](#) (a central bank)

Here in Hawai`i, with a high record of foreclosures, many families have learned of the destructive nature of credit default swaps, profits made from foreclosing on local and military families, and the difficulty of simply faxing documents to mainland loan servicers and loan modification centers.

In North Dakota, Legislators, bankers and BND worked together to successfully develop and implement the BND Rural Mortgage Loan Origination Program authorized in the 2011 Legislative Session which allows BND to originate residential real estate loans. It was the first time BND had been in the home mortgage loan origination business since the 1970s. As BND celebrates its 100th anniversary, lenders can refer their customers to BND to originate a home mortgage or

they can choose to originate a home mortgage and sell the loan to BND as their secondary market option.

Similarly, a Bank of the State of Hawai`i could meaningfully help local and military families facing foreclosure by negotiating with their mortgage company, offering to buy the mortgages for cents on the dollar, “cleansing” the defective title done by robo-signing and other failures in the chain of title, and selling the house back to the families at an affordable price, thus averting the risk of loss of their residences and homelessness.

For these reasons, we urge you to vote favorably on this bill directing the Department of Commerce and Consumer Affairs to conduct a comprehensive review of relevant state laws to develop legislation to establish a state-operated bank of the State of Hawaii; and to appropriating funds to conduct the review.

Mahalo for this opportunity to testify,

/s/ Melodie Aduja

Environmental Caucus of the
Democratic Party of Hawai`i

<https://businesstech.co.za/news/banking/374120/south-africa-to-get-a-new-state-owned-bank-and-investment-fund/>

<https://www.civilbeat.org/2012/03/15305-state-bank-concept-takes-hold-in-hawaii/>

<https://thebndstory.nd.gov/an-agile-partner/an-economic-development-bank/>

https://en.wikipedia.org/wiki/Bank_of_North_Dakota

https://en.wikipedia.org/wiki/State_bank