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TO THE
HOUSE COMMITTEE ON
FINANCE

THE TWENTY-SEVENTH STATE LEGISLATURE
REGULAR SESSION OF 2013

Thursday, February 14, 2013
3:30 p.m

TESTIMONY ON H.B. NO. 840, H.D. 1
RELATING TO FINANCIAL INSTITUTIONS

THE HONORABLE SYLVIA LUKE, CHAIR,
AND MEMBERS OF THE COMMITTEE:

My name is Iris Ikeda Catalani, Commissioner of Financial Institutions ("Commissioner"), testifying on behalf of the Department of Commerce and Consumer Affairs ("DCCA") in strong support of administration bill, House Bill No. 840 H.D. 1.

This bill has two primary purposes. First, it modernizes the State's Financial Institutions law, Chapter 412, Hawaii Revised Statutes ("HRS"), in light of changes to federal banking laws including the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Second, it adjusts fees for financial institutions to reflect the

additional regulation and monitoring required of the Division of Financial Institutions ("Division" or "DFI") as a result of changes to the law, and increasing sophistication of the financial institutions industry.

The last comprehensive review of financial institutions laws was in 1993. In the summer of 2012, the Commissioner conducted meetings with representatives of the financial institutions industry for the purpose of reviewing and modernizing the State's banking laws to reflect changes in federal law. This bill is the result of those meetings.

Self-Funding Requirement Necessitates Requested Fee Changes

To provide context for the fee changes proposed by this bill, the Commissioner submits the following. The Division is responsible for the licensure, examination and supervision of state-chartered and licensed banks, trust companies, savings and loan associations, financial services loan companies, credit unions, escrow depositories, money transmitters, mortgage servicers, mortgage loan originators and mortgage loan originator companies. As a special-funded program, the Division is responsible for generating sufficient revenues to fully fund its operations. As such, the Division is tasked with the responsibility of aligning its revenues with expenditures so as to ensure that it is self-sustaining. To fully meet its total operating costs, the program needs to manage a cash reserve that is sufficient to meet direct operating costs, overhead costs and unanticipated contingency costs/accrued liabilities.

Overall, the Division's revenues are inadequate to fully fund its current operations, including the filling of all authorized positions and covering the Division's shared of the departmental overhead. In recent years, the Division has taken advantage of vacancy and furlough savings to temporarily address the cash reserve concerns. However, with the increased responsibilities resulting from changes in federal laws and sophistication of the financial institution industry, the Division's workload has increased substantially requiring the filling of all authorized positions. Notwithstanding the extraordinary efforts of Division staff, the Division is currently backlogged between 120 and 180 days in its licensing work due to understaffing. The Division appreciates the Legislature's authorization of 34 staff positions to carry out its responsibilities. However, the revenue stream from fees generated from the current fee structure as set by statute is sufficient to sustain only 28 positions. Consequently, six authorized positions, all of which are "permanent," are vacant. So while there is a clear need for additional staff to appropriately carry out the Division's mandates and to protect the public, the Division is not in a position to cover the ongoing cost of these permanent positions until its revenue streams are changed and made sustainable.

Division's staff vacancies adversely affect the State's economy and the public's interests in a number of ways. Businesses that are otherwise ready to open may have to wait months to obtain approval on their initial license applications, despite best efforts of the Division and its staff. They must postpone hiring employees and generating

revenue that would increase the State's tax base. Licensees who do not apply for license renewals well before the end of the year may end up in a similar predicament, unable to lawfully conduct business after their license expires, and in limbo until the Division can confirm satisfaction of license renewal requirements and issue a license renewal. For the public, the Division's personnel shortage means potentially months of delay in its examination of licensees which handle billions of dollars of consumer financial transactions annually. It also potentially means months of delay in the Division's discovery of licensees that could benefit from the Division's assistance and monitoring to help them restore their financial viability and strength. In an extreme case, a staff shortage could mean that the Division cannot discover and investigate questionable licensee conduct and circumstances in time to avert massive financial harm to the public.

A guiding principle for the Department's special-funded programs in maintaining the delicate balance between fee setting and cash reserve management is that the revenues from each of program must be sufficient to cover the Division's cost of operating that program. The Division estimates that it will need additional revenues of approximately $500,000 a year to adequately meet its cash reserves needed to support the Division's operations and facilitate its ability to appropriately carry out its mission.

An analysis of program costs as compared to program revenues shows a deficit in FY11 and FY12 for the financial institutions program:

Financial Institutions Program	FY11	FY12
Total Program Cost to Division	$1,446,353	$1,502,562
Less Program Revenues	$341,165	$332,213
Surplus/(Deficit)	($1,105,188)	($1,170,349)

In addition to the revenue stream from fees that are statutorily set, the Division receives a portion of the franchise tax paid by the financial institutions and the mortgage loan originators and mortgage loan originator companies. The timing of the receipt of the franchise tax revenue creates a cash flow problem for the Division. Section 241-7, HRS, provides for the deposit of the franchise tax revenue by June 30 of each fiscal year. As such, adequate cash reserves need to be maintained in order to fund the annual program costs while awaiting the deposit of the monies.

The Division anticipates that the revenues from the financial institution program will bring in approximately $272,590 a year with the adjusted fee schedule. We believe that with a fully staffed Division, we can provide the services requested and expected by our financial institution licensees as well as provide the appropriate oversight for consumers.

Part I - Clarification of Existing Law

Part I of the bill adds some new definitions and amends some existing definitions to reflect changes in federal laws over the last 20 years.

Part II – New Fee Structure – Recommended Effective Date January 1, 2014

As a result of federal laws enacted and amended over recent years, the Division must exercise heightened supervision, regulation and examination over state chartered financial institutions. We provide oversight for consumer protection with our federal regulator partners, which include a new federal regulatory partner, the Consumer Financial Protection Bureau.

The Division proposes to adjust the fee schedule in two ways (1) by replacing the "ala carte" type fee structure with an annual assessment and (2) adjusting the application fees to reflect the review and analysis time by the Division. The annual assessment fee schedule is used by at least 48 other states and the FDIC for insurance assessment and by the OCC (Office of the Comptroller). The annual assessment will cover all services for a year including the annual examination and investigations.

Section 10 establishes a new fee structure for financial institutions, which the Division recommends be made effective January 1, 2014. The request to delay implementation in the fee structure is twofold: (1) to allow the small financial institutions in particular to be able to budget for the increase in fees and (2) the annual fee are assessed in June, thus, we would have already collected for the year by the time the proposed bill is passed. The new structure is based on an institution's total assets, a term that is defined, and consists of a scaled flat fee plus a percentage of total assets. There is a cap on fees for the very largest institutions. Currently, the law allows for only

a nominal flat fee and a per branch fee. Basing financial institution fees on asset size will bring Hawaii in step with the great majority of states. This change also recognizes that larger financial institutions have more complexity to its organization both in terms of review of its financial statements and examination of its safety and soundness issues and use more of the Division’s resources.

Section 10 also specifies fees for certain applications and certifications. This is to ensure that initial costs to the Division of reviewing these applications and the cost of certifications are covered fairly by the institutions using the Division's resources.

Section 11 makes it mandatory, rather than permissive, for the Commissioner to charge a financial institution for travel, per diem, mileage and other reasonable expenses incurred in connection with an examination and investigation.

Conforming amendments to delete references to specific fees are addressed in Sections 11 to 25.

Part III – Interim Fee Structure – Recommended Effective on Approval

Part III of the bill, Section 26, basically mirrors the new fee structure for applications set out in Section 10. This is an interim fee schedule that is needed so that the change in application fees will be effective on the bill’s approval, rather than waiting until the effective date of the new fee structure of Part II.

Part IV – Effective Dates

We recommend that Part III, the interim fee structure, be made effective on approval (rather than on January 1, 2014); and H.D. 1 appropriately provides a repeal date for Part III of January 1, 2014. We also recommend that Part II be made effective on January 1, 2014 (rather than on January 1, 2112), which is the repeal date of Part III. As stated above, the interim fee structure of Part III is needed so that the change in application fees will be effective on the bill's approval, rather than waiting until the new fee structure of Part II comes into effect.

For these reasons, DFI strongly supports this administration bill, H.B. No. 840, H.D. 1, and respectfully asks that the measure be passed with amendments to the Part IV effective dates, as recommended in our testimony.

Thank you for the opportunity to testify. I would be pleased to respond to any questions you may have.

Hawaii Bankers Association

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Presentation to
Committee on Finance
February 14, 2013 at 3:30 pm
State Capitol Conference Room 308

Testimony in SUPPORT of H. B. 840

TO: The Honorable Sylvia Luke, Chair
The Honorable Scott Y. Nishimoto, Vice Chair
The Honorable Aaron Ling Johanson, Vice Chair
Members of the Committee

My name is Neal Okabayashi from First Hawaiian Bank, and I testify for the Hawaii Bankers Association, a trade association of local banks, whose deposits are insured by the Federal Deposit Insurance Corporation.

Our present Code of Financial Institutions was enacted in 1993 and since that time, many new banking developments have come to pass including the Gramm-Leach-Bliley Act and more recently, the Dodd-Frank Act. In addition innovative technology had led to electronic banking, stored value cards and concern for the unbanked and underbanked who can be well-served by stored value cards. Thus, an effort to modernize our Code to be up-to-date with current federal law and FDIC regulations was spearheaded by our commissioner of financial institutions, and HBA lauds her for her efforts.

These changes will enable state chartered banks to keep pace with our brethren who are chartered by the federal government (such as American Savings and Hawaii National Bank) who operate under federal laws which have kept pace with modern banking.

Thus, in the interest of a level playing field and a more current banking law, HBA supports sections 1 through 6 of HB 840.

We would be happy to answer any questions the Committee may have.

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February 14, 2013

Rep. Sylvia Luke, Chair
and members of the House Committee on Finance
Hawaii State Capitol
Honolulu, Hawaii 96813

Re: **House Bill 840, HD 1 (Financial Institutions)**
Hearing Date/Time: Thursday, February 14, 2013, 3:30 p.m.

I am Marvin Dang, the attorney for the **Hawaii Financial Services Association** ("HFSA"). The HFSA is a trade association for Hawaii's consumer credit industry. Its members include Hawaii financial services loan companies (which make mortgage loans and other loans, and which are regulated by the Hawaii Commissioner of Financial Institutions), mortgage lenders, and financial institutions.

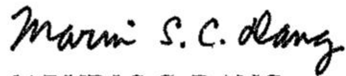
The HFSA supports Sections 8 and 9 of this Bill, but takes no position on the other sections.

The purposes of this Bill are to: (1) replace individual fees (for specific regulatory items)with one assessment for Hawaii banks and nondepositories, (2) increase and clarify bank powers, and (3) clarify the authority of the Commissioner of Financial Institutions.

We support Sections 8 and 9 of this Bill. Those Sections affect financial services loan companies by giving them the power to charge a $10 fee to process a draft written below the minimum amount established on an open end loan (Section 8) and by clarifying the credit exposure for derivatives (Section 9).

We do not take a position on the other sections of this Bill.

Thank you for considering our testimony.



MARVIN S.C. DANG
Attorney for Hawaii Financial Services Association

(MSCD/hfsa)