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**TO THE
HOUSE COMMITTEE ON
FINANCE**

**THE TWENTY-SEVENTH STATE LEGISLATURE
REGULAR SESSION OF 2013**

Wednesday, March 27, 2013
4:45 p.m.

**TESTIMONY ON S.B. NO. 1069, S.D. 2, H.D. 1
RELATING TO MORTGAGE LOAN ORIGINATION**

**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, Senate Bill No. 1069, S.D. 2, H.D. 1. This bill primarily focuses on amendments to Chapter 454F of the Hawaii Revised Statutes ("HRS"), the "Secure and Fair Enforcement for Mortgage Licensing Act."

This bill has two major purposes: (1) it clarifies licensure requirements for mortgage loan originators and mortgage loan originator companies, and for mortgage servicer companies conducting mortgage loan origination activity (collectively, “Chapter 454F licensees”), and (2) it adjusts fees for the mortgage loan origination licensees, and it establishes fees for mortgage servicer companies that conduct mortgage loan origination activities. Fee adjustments were agreed to by the mortgage loan origination industry representatives last year, and are needed to close the gap on the deficit that the Division of Financial Institutions (“Division” or “DFI”) has been covering to meet its statutorily mandated duties to oversee and regulate its licensees.

Modernization of the Law

- NMLS Licensing System – Mortgage loan originator and mortgage loan originator company licensees already register with the “Nationwide Mortgage Licensing System,” pursuant to Hawaii law. This is a cost-effective way to manage the Division’s Chapter 454F licensees and other financial services providers, and will enable the Division to use the electronic method to review, oversee and license its licensees.
 - Sections 2 and 20: The bill globally updates the system’s name as it is now known as “NMLS,” and it defines NMLS.

- Section 7: Authorizes the Commissioner to enter into agreements with NMLS or other entities to use NMLS to collect and maintain records and process licensee fees.
- Section 16: Clarifies that reports of condition that licensees submit to NMLS, shall be provided quarterly.
- The NMLS system benefits consumers who can see which companies are licensed in Hawaii through the NMLS consumer access page.
- The on-line application and renewal process will benefit licensees who conduct mortgage loan origination activities in more than one state as they will have the ability to use a nationwide application. As a note, the Division must continue to ask for items outside of the NMLS for the state specific information required by our Hawaii law.
- Mortgage Servicer Licensees
 - Sections 2, 6 and 12: The bill refines the definition of a "mortgage servicer company" for purposes of Chapter 454F, and requires such a company to be registered and licensed through NMLS.
 - Sections 10, 18 and 19: License renewal requirements, fees, and mortgage loan recovery fund contributions are specified.
 - Section 12: Authorizes the Commissioner to establish licensing requirements for mortgage servicer companies by administrative rule.

- Branch Supervision – Section 13: Clarifies that a mortgage loan origination company shall have a branch manager physically present its Hawaii headquarters; and that a thirty-day advance notice is required for relocating an office of a mortgage loan originator company.
- Education – Sections 8, 10 and 11: Amends pre-license and license renewal education requirements for mortgage loan origination professionals to stay in compliance with State and federal law, which is frequently changing.
- Clarifying Amendments – Sections 2 and 4: Clarifies a number of terms that are already used in Chapter 454F, including the following:
 - “Exempt registered mortgage loan originator” is amended to remove from the definition an individual who is an employee of an insured depository institution subsidiary.
 - “Licensee” is amended to include certain mortgage servicer companies and exclude certain nonprofits.
 - “Mortgage loan originator” is amended to include an individual who offers or negotiates a mortgage loan secured on specified family property, and who does so no more than three times a year.
 - Presumption of Control – Section 4: Narrows the term to apply to certain persons with specified voting rights and the power to direct the sale of a

class of voting securities of the company. Extends the concept to apply to
a mortgage servicer company.

These changes will help avoid ambiguity as to the Commissioner's authority and
duties, and licensee responsibilities.

- Housekeeping Amendments – Have been added for conformity.

Changes Agreed to by the Industry

Representatives of the mortgage loan origination industry met with the Commissioner in 2012, and agreed to the fee adjustments for their industry set out in S.B. 1069 as originally introduced. DFI has further regulatory responsibilities over these licensees resulting from federal amendments to Privacy Laws, Bank Secrecy Act/Anti-Money Laundering Program laws, and Consumer Financial Protection Bureau guidance and regulations. The fee structure is adjusted by this bill to take into account the additional supervision, regulation, and examination of these licensees. Adjustments include the following:

- Section 15: The hourly fee for examination of a Chapter 454F licensee and others subject to the chapter is adjusted from \$40 to \$60 to be the same as the other industries we supervise and examine.
- Section 18: Mortgage loan originator fees are adjusted for the initial application and annual license renewal including the reduced fees for sole proprietor mortgage loan originators. A \$35 fee is added for processing a control person.

Self-Funding Requirement Necessitates Requested Fee Changes

The chart below shows that the mortgage loan origination program ran increasing substantial deficits in FY11 and FY12.

MORTGAGE LOAN ORIGINATION PROGRAM	FY11	FY12
Program Cost to Division	\$932,161	\$716,791

Less Program Revenues	\$760,021	\$622,470
Program Deficit to Division	(\$172,140)	(\$94,321)

The Division anticipates that the mortgage loan origination program will bring in approximately \$10,000 of additional revenue annually under the original fee adjustment request. Although the amount of the anticipated revenue will not cover the cost of supervision, it will help defray some of the costs of oversight.

DCCA has been financially self-sufficient since 1999. Its operations are not funded by the Legislature's general fund, but instead by the persons and entities who are regulated by DCCA or who receive services from the Department.

As you will see in the chart below, current projections are that at the end of FY15, the Division will have a reserve of just over \$600,000, less than two month's operating expenses. By the end of FY16, the Division will be unable to meet payroll, and will actually be short by \$212,838:

DFI CASH FLOW PROJECTION				
Source	FY13 (estimated)	FY14 (estimated)	FY15 (estimated)	FY16 (estimated)
Beginning Cash Balance	5,043,246	4,265,971	3,450,942	2,629,452
Plus Program Generated Revenues	1,230,700	1,190,400	1,190,800	1,170,000
*Less Expenditures	4,007,975	4,005,429	4,012,290	4,012,290
Cash Balance @ June 30	2,265,971	1,450,942	629,452	(212,838)

Plus Franchise Tax (received in late July @ beginning of new FY)	2,000,000	2,000,000	2,000,000	2,000,000
Equals Ending Cash Balance	4,265,971	3,450,942	2,629,452	1,787,162

Figures are based on Report on Non-General Fund Information for Submittal to the 2013 Legislature, Program ID CCA-104, Fund Name CRF-Financial Institutions. *Expenditures are based on Appropriation Ceiling and include 34 authorized permanent staff positions and DFI share of DCCA overhead.

The franchise tax¹ infuses funds critically needed by the Division in late July of each year, for the **previous** fiscal year. During the fiscal year, DFI spends the franchise tax allocation on salaries and expenses, and it relies on franchise tax revenues being re-infused in July of the following fiscal year. The Division needs to have sufficient cash reserves on hand to fund its annual program costs while awaiting deposit of the franchise tax monies.

The chart above anticipates that the Division is fully staffed with the 34 permanent positions that the Legislature has authorized. The Division has been experiencing an increased workload between the greater oversight and regulatory responsibilities it has been given, changes in federal laws, and sophistication of the financial institution industry. **Since 2006, the Division has been given three new programs which do not collect adequate revenue to appropriately supervise those programs.** Below is a list of how the Division has operated within its budget:

- The Division has refrained from filling its six staff vacancies.

¹ This is a tax paid by the financial institutions, and the mortgage loan originators and mortgage loan originator companies, deposited with the director of Finance by June 30 of each fiscal year, pursuant to HRS sec. 241-7.

- The Division has a current 120 to 180 day backlog in processing licensing work.
 - Delay in the Division's licensing and examination work is contrary to the best interests of consumers and business.
 - It means delays in opening of new businesses and their hiring of employees which would contribute to the State's economy.
 - It means a delay in issuing license renewals rendering licensees with expired licenses unable to lawfully conduct business.
 - We have not been able to fully examine our licensees which handle billions of dollars of consumer financial transactions annually, delaying the discovery of licensees that could benefit from the Division's assistance and monitoring to help them restore their financial viability and strength.
 - Delays also mean questionable licensee conduct goes undiscovered in time to avert massive financial harm to the public.

The Division would like to have a reasonable reserve fund²; it is currently headed toward a fiscal cliff absent an increase in revenues. It cannot expect to receive funding in excess of what its own programs have generated, from funds generated by programs of other divisions that are held in the DCCA Compliance Trust Fund.³

² The Hawaii Supreme Court has recognized that it is reasonable for a regulatory division to have a reserve fund, which can be essential to the Division's regulatory function. See Hawaii Insurers Council v. Lingle, 201 P.3d 564, 580 (2008) (hereinafter "HIC v. Lingle").

³ See HIC v. Lingle, 201 P.2d at 580.

Proper Staffing Levels Are Required to Maintain Appropriate Supervision

A revenue shortfall in one Division program impacts all of its other programs. The shortfall keeps the Division from hiring staff. Yet industry licensees and applicants still need to be served. We believe that with a fully staffed Division, we can provide the services requested and expected by our mortgage loan origination licensees as well as provide the appropriate oversight for consumers.

Amendments requested

DFI requests that the following language for sole proprietors be restored in this version of the bill. We believe there was a misunderstanding during the discussion of this bill to allow sole proprietors to renew their license and be subject to the same licensing standards as other mortgage loan originators.

(b) A sole proprietor mortgage loan originator shall pay an initial application fee of \$35 to obtain and maintain a valid sole proprietor mortgage loan originator license.

(2) Annual license renewal fee of \$35;

(3) Reinstatement fee of \$100;

(4) Late fee of \$25 per day; and

(5) Criminal background check fee of \$35, or of an amount determined by the commissioner by rule pursuant to chapter 91.

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DFI strongly supports this administration bill, Senate Bill No. 1069, S.D. 2, H.D. 1, and respectfully requests that it be passed out of committee.

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