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TO THE
HOUSE COMMITTEE ON
FINANCE

THE TWENTY-SEVENTH STATE LEGISLATURE
REGULAR SESSION OF 2013

March 27, 2013
4:45 p.m.

TESTIMONY ON S.B. NO. 1070, S.D. 2, H.D. 1
RELATING TO MORTGAGE SERVICERS

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. 1070, S.D. 2, H.D. 1.

This bill has two primary purposes: (1) it authorizes the Commissioner to examine mortgage servicers, and provides realistic examination and investigation tools, and (2) it adjusts the fees for mortgage servicer licensees registering through the NMLS system used by the Division of Financial Institutions, which regulates mortgage servicers under Chapter 454M, Hawaii Revised Statutes (“HRS”).

The need for meaningful mortgage servicer oversight is evident from the failure of the nation's mortgage loan systems, and in the wake of last year’s landmark $25 billion joint state-federal agreement with the nation’s five largest mortgage servicers over foreclosure abuses and fraud, and unacceptable nationwide mortgage servicing practices. Since these events, there has been a reevaluation of laws by every state and the federal government in an effort to address breakdowns in the mortgage servicing industry and better protect consumers.

In Hawaii, mortgage servicers serviced over 35,000 residential loans with an aggregate value of $9.78 billion, according to 2012 licensee renewal data. Mortgage servicers are responsible for billing and collecting mortgage payments from residential homeowner borrowers, and transmitting payments to owners of the mortgage loans. They also typically handle customer service, escrow accounts, collections, loan modifications, and foreclosures.

We expect the mortgage servicers that we regulate to operate with a high level of integrity. Still, in view of what has been learned from the nationwide financial crisis, we submit that it is both realistic and important for the Commissioner to have the investigation tools that this bill provides, in order to protect consumers. As just one example, the federal government recently prosecuted a mainland company alleging that it had conducted a scheme to prepare and file more than one million fraudulently signed and notarized mortgage-related documents, many of which were used in foreclosure proceedings to force homeowners out of their homes. The Commissioner should have the authority to examine mortgage servicers suspected of improper conduct without having to await a consumer complaint, and the Commissioner should have the proper tools to conduct a meaningful investigation.

Modernization of the Law

- Section 1: Authorizes the Commissioner to conduct mortgage servicer examinations and investigations that do not require initiation by a consumer complaint. **Action by a mortgage servicer can potentially cause a consumer to lose his or her home. With this much at stake, the Commissioner needs the ability to examine and investigate these licensees to at least the same extent as the loan originators who help the consumer finance the home purchase.**
- Section 1: Also authorizes the Commissioner to charge an examination and investigation fee and reasonable expenses incurred in the process. Only the licensee examined will be charged for the.
- Sections 2, 3 and 4: Update HRS Chapter 454M by defining and changing references to the “Nationwide Mortgage Licensing System,” to “NMLS,” which is

the system's new name. NMLS changed its name to reflect that other industries are using the database.

- Section 3: Adjusts licensure fees to take into account the fees that NMLS charges the State for using NMLS in connection with mortgage servicer licensure.
  - Using the NMLS electronic database should create efficiencies and savings for the Division in overseeing and licensing mortgage servicers, enable the public to easily determine whether a mortgage servicer is licensed, and save time for licensees who conduct mortgage servicing activities in more than one state as they can use a nationwide application.
  - Note that the Division must continue to ask for items outside of the NMLS for the state specific information required by our Hawaii law.
- Section 5: Housekeeping amendments reflect the change in the federal regulator from the Housing & Urban Development Department to the Consumer Financial Protection Bureau ("CFPB").
- Section 6: Extends existing licenses for current licensees until December 31, 2013, conforming to the renewal schedule used by the NMLS.

Self-Funding Requirement Necessitates Requested Fee Changes

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

MORTGAGE SERVICERS PROGRAM	FY11	FY12
Program Cost to Division	$114,265	$197,942
Less Program Revenues	$27,500	$24,000
Program Deficit to Division	($86,765)	($173,942)

The Division anticipates that the mortgage servicers program will bring in approximately $7,875 of additional revenue annually, with the adjusted fee schedule and amendments requested. Although the amount of the anticipated revenue will not cover the cost of regulation, 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 tax[1] infuses funds critically needed by the Division in <u>late July</u> 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 mortgage servicers 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.
- 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.

[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 would like to have a reasonable reserve fund[2]; 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]

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 servicer licensees as well as provide the appropriate oversight for consumers.

DFI strongly supports this administration bill, Senate Bill No. 1070, S.D. 2, H.D. 1, and respectfully asks that the measure be passed out of committee.

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

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[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) ("HIC v. Lingle").

[3] *See* HIC v. Lingle, 201 P.2d at 580.