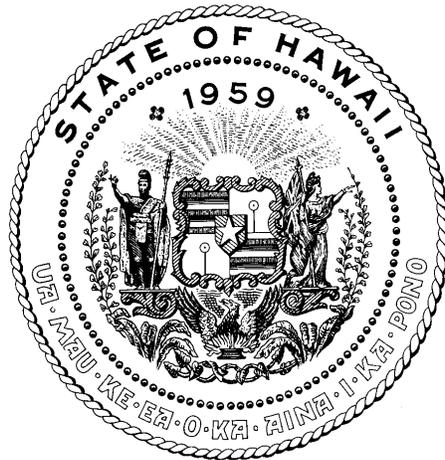


Annual Compliance Resolution Fund Report



**DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS
STATE OF HAWAII
SUBMITTED DECEMBER 2018**

DIVISION OF FINANCIAL INSTITUTIONS (DFI)

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OVERVIEW

The Division of Financial Institutions (DFI): (1) addresses the safety and soundness of state-chartered and state-licensed financial institutions; and (2) ensures regulatory compliance by state-licensed financial institutions, escrow depositories, money transmitters, mortgage servicers, mortgage loan originators, and mortgage loan originator companies by fairly administering applicable statutes and rules to protect the rights and funds of depositors, borrowers, consumers, and other members of the public. To effectively regulate a growing and diverse group of industries and implement state and federal regulatory requirements, the DFI made changes to its licensing and examination programs to focus its resources on risk-based supervision.

The DFI provides regulatory oversight for the State's financial service providers, which include both bank and nonbank companies. The DFI provides supervision, regulation, and examination of all Hawaii state-chartered and state-licensed financial institutions, including banks, foreign banking agencies and representative offices, savings banks, trust companies, financial services loan companies (both depository and non-depository), and credit unions. In supervising financial institutions authorized to take deposits, the DFI works closely with the Federal Deposit Insurance Corporation (FDIC), Federal Reserve Bank of San Francisco (FRB), CFPB, and National Credit Union Administration (NCUA).

The major functions of the DFI are to:

- Charter, supervise, regulate, and examine all state banks and credit unions, foreign bank branches, agencies and representative offices, and intra-Pacific branches.
- License, supervise, regulate, and examine non-depository companies including escrow depositories, money transmitters, mortgage loan originators, mortgage loan originator companies, and mortgage loan originator branches and mortgage servicer companies.
- Accept and investigate complaints by consumers.

The DFI is recognized by two accreditation organizations as providing the highest standards of training for its staff and for appropriately supervising and examining chartered and licensed companies and individuals. The DFI was first accredited by the Conference of State Bank Supervisors (CSBS) in 1990 and reaccredited in 1995, 2000, 2005, 2012¹, and 2018. The CSBS accreditation program sets high standards for state banking regulators nationwide. Forty-seven of 52 states² meet CSBS accreditation requirements.

¹ Hawaii did not seek reaccreditation in 2010. With the new commissioner appointed in 2011, and updates made to the banking supervision, regulation, and examination, the DFI received accreditation in 2012.

² Includes the District of Columbia and Puerto Rico.

In 2Q FY 2015, the DFI was the eighteenth state in the nation to be accredited by the CSBS/AARMR³ for mortgage supervision. The CSBS/AARMR accreditation program sets high standards for state mortgage regulators nationwide. Currently, 26 of 66 mortgage regulatory agencies meet CSBS/AARMR accreditation standards. The accreditation program includes the mortgage loan originator, mortgage loan originator companies, and mortgage servicer programs. Hawaii was also recognized for its robust regulatory scheme and oversight, as well its mature examination program.⁴

The following is the DFI's contact information:

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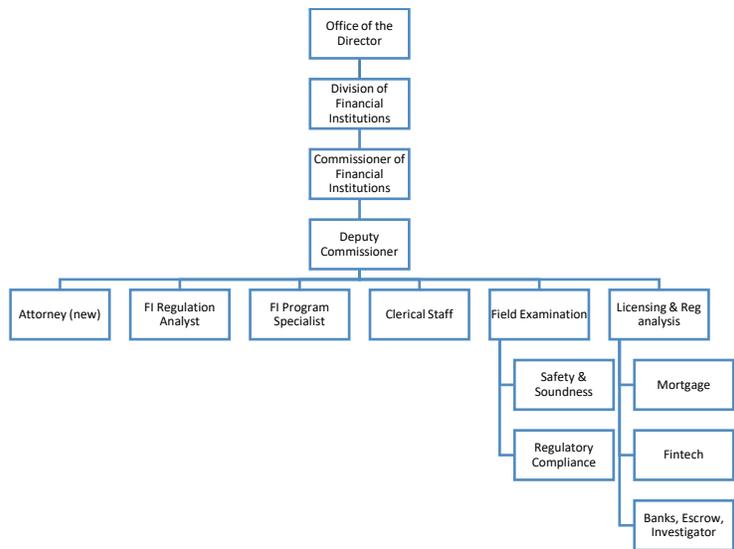
Phone: (808) 586-2820

³ The AARMR is a trade organization for mortgage regulators.

⁴ In 2009, the Hawaii Secure and Fair Enforcement for Mortgage Licensing, or SAFE, Act was passed, giving the DFI authority to supervise, regulate, and examine mortgage loan originators and mortgage loan originator companies. In late 2010/early 2011, the DFI began its supervision. From 2011 to 2012, the DFI provided training to the industry. In 2013, the DFI began its examination program.

COMPOSITION

The DFI is led by the Commissioner of Financial Institutions, who is assisted by the **Administrative Section**, which has a deputy commissioner, a staff attorney, a specialist, a regulation analyst, and secretarial staff supervised by the secretary of the division. This section coordinates and facilitates activities within the DFI, with other divisions, and with other state and federal agencies regarding regulatory and supervisory oversight issues.



The DFI is divided into two branches:

The **Field Examination Branch** is composed of financial institution examiners and supervised by a branch manager. The branch is responsible for on-site and off-site examinations of all state-chartered and state-licensed financial institutions. Examinations, unlike accounting audits, are forward-looking and risk-based reviews of factors underlying the safety and soundness of financial institutions. For example, examiners not only evaluate existing and projected financial information, but also assess the effectiveness of management, its policies, and implementation of those policies in administering the institution’s risk management programs and practices. The branch is divided into two sections: one section focuses on the safety and soundness of state-chartered banks, credit unions, and money transmitters, while the other section focuses on compliance with federal and state regulatory laws and guidance for mortgage-related industries.

The **Licensing and Regulatory Analysis Branch** is composed of financial institution examiners and supervised by a branch manager. The branch is responsible for licensing activities and other regulatory approvals, the quarterly off-site monitoring program, responding to complaints and inquiries from consumers and licensees, and investigating alleged violations of state and federal laws. Licensing activities include reviewing and analyzing all applications for new financial institutions (bank and nonbank), opening, relocating, or closing branches, and adding new or unique services to determine whether consumers may be harmed by the action of any licensee. The branch reviews all license renewals for state and federal compliance before issuing an approval. The branch has two sections: one section focuses on emerging financial technology

(fintech) companies including money transmitters, while the other section focuses on the mortgage industry, including mortgage loan originators, mortgage loan originator companies, and mortgage servicers. This branch also oversees banks and escrow depositories and includes an investigator who conducts investigations in all industries supervised by the DFI.

GOALS AND OBJECTIVES

Goals

The DFI's mission reflects its role in protecting consumers and providing an avenue for companies to provide products and services to Hawaii's residents. The following are the DFI's goals and objectives:

- (1) Maintain public confidence and trust in the financial system in a changing environment.
 - The DFI does not receive any general funds. Instead, the division receives funding from its chartered and licensed companies and individuals. The DFI operates like a business, as it balances revenues and expenses to provide oversight and supervision for the benefit of Hawaii's residents.
 - The DFI reviews and proposes changes to its laws to appropriately meet the everchanging environment in which it functions. The innovative business models and functions of licensees have changed the landscape of compliance to become complex and multifaceted. Instant fulfillment of services has become the norm for consumers, and the DFI struggles to continue maintaining proper supervision of licensees.
 - The DFI provides joint regulation, supervision, and examination of state-chartered financial institutions. The DFI is the primary regulator for non-depository industries.

- (2) Have an effective and collaborative workforce with satisfied and valued employees who see the DFI and DCCA as their employer of choice.
 - Since 2011, the DFI processes its work through electronic means and continues to expand the use of technology in processing work from applicants and licensees. Licensees apply for licenses, renewals, and any changes through a secure electronic channel. All processing of applications and requests occurs electronically. Examinations are also conducted electronically, where licensees provide examination documents through a secure channel. Examiners spend less time on-site with the licensee, saving money for the licensee and travel times by the examiners. The DFI still accepts paper inquiries and complaints from consumers, although more consumers have taken advantage of the DFI's online consumer complaint process.
 - The DFI has been developing a career path for employees to advance and retain employees. The DFI has been successful in recruiting new employees and retaining employees once trained.
 - The DFI leverages its resources with other state and federal agencies to provide oversight over state-chartered and licensed companies. This coordination involves communication skills to efficiently discuss and take appropriate action on licensees.

- (3) Have effective and efficient operations and programs.

- The DFI re-organized its licensing branch to create two distinct branches.
- The DFI continues to work with a vendor to implement a workflow process that would include a searchable database.

(4) Achieve the DFI's strategic objectives.

- Over the last five years, the DFI's staffing has undergone a tremendous change, with the addition of 23 new staff members who work with technology to meet the DFI's goals and objectives. In FY 2018, the DFI added one new examiner. The DFI's goals and objectives center on the orientation, training, and effective deployment of its examiners and providing best practices to licensees in a professional manner. Federal training programs administered by the FDIC and the Federal Reserve System are regularly used for this purpose, as are web-based programs provided by the CSBS, Risk Management Association, and Hawaii Bankers Association. On-the-job training is also a valuable component of the training plan. The DFI's goals also focus on recruiting new staff who will be able to adjust to the rapidly changing landscape of the financial services industry. New financial service products continue to be created, modified, and initiated by licensees regulated and supervised by the DFI. Delivery methods have also expanded through use of the internet, cellular phones, and other mobile devices, as well as their impact upon cybersecurity. Consequently, it is challenging for examiners to stay up-to-date with the latest iteration of products, services, and delivery methods.

Strategic Plan

As a part of the CSBS accreditation process, the DFI established a strategic plan and developed policies and operating guidelines to achieve plan objectives. The following is the DFI's strategic plan, which is updated annually:

- Stay relevant in a changing environment.
- Provide value for the services the division offers.
- Expand employees' respective skill sets.
- Embrace the new regulatory and compliance environment.
- Deliver effective and timely services.
- Communicate respectfully, timely, and meaningfully.

This strategic plan guides the DFI's objectives, and the policies to accomplish those objectives are embedded in its policy and operating manuals.

Action Plan

The DFI's action plan is built around its strategic plan. The DFI has achieved or continues to work toward completion of its strategic goals. In FY 2018, the DFI revisited its strategic plan for the next five years by setting new goals, objectives, and action plans. The DFI continues to explore various technology to improve its efficiency, databases, and outreach to consumers and licensees. In addition, the DFI has joined other states in the supervisory oversight and examination of non-depository companies who conduct business in the U.S. and globally.

Performance Measurement

The DFI measures performance in two ways. The first measurement is empirical and involves financial and examination-based measurements of the fiscal health and regulatory compliance of DFI-regulated financial institutions. This measurement is critical, especially in the current climate of global turmoil in the financial services industry, and demonstrates the DFI's key area of responsibility: to ensure the safety and soundness of Hawaii-chartered and licensed financial institutions. The second measurement involves the DFI's internal throughput, i.e., how many complaints have been answered, how many applications have been processed, etc. This measurement is difficult to quantify, since the increasing complexity of inquiries makes reviewing applications and complaints and conducting investigations time- and resource-intensive. This measurement provides the DFI with insight into how companies use innovations and solutions to address financial services. The DFI is mindful that these measurements do not comprehensively indicate the division's efforts or the regulatory activity occurring at the state and federal level.

ACCOMPLISHMENTS

(1) Special projects

After passage of Hawaii's medical cannabis dispensary law, the DFI conducted research for two years to find a banking solution for medical cannabis dispensaries. Through an arrangement with a Colorado credit union, the Commissioner of Financial Institutions provided an option for safe and sound banking services to the medical dispensaries. This arrangement is temporary until a Hawaii-based financial institution is able to provide banking services to the medical dispensaries. The Commissioner of Financial Institutions continues to provide training and oversight over financial institutions that weigh the risks associated with violating the federal laws regarding the Controlled Substances Act and the Bank Secrecy Act. The Commissioner of Financial Institutions continues to be a leader among the financial institution regulators, speaking at various seminars, symposiums, and conferences about banking and cannabis businesses.

(2) Effective supervision

Hawaii has six Hawaii state-chartered banks, two out-of-state chartered banks (CA and WA), two national banks, one intra-Pacific branch, and one foreign bank. The DFI directly supervises the six Hawaii state-chartered banks, oversees with its sister states the two out-of-state chartered banks, and oversees the one foreign bank. All state-chartered banks are operating in a safe and sound manner and complying with regulatory laws and guidance. As of Q1 FY 2019, all state-chartered banks have reported increased earnings due in part to increased loan growth, but the primary reason for increased earnings is the double-digit decrease in tax rates. The DFI conducts multi-state examinations with other states for non-depository companies who conduct business in the U.S. and abroad.

As the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) are implemented by the various federal regulatory agencies, the DFI will also meet the needs of informing and supervising our state-chartered and state-licensed financial institutions to protect consumers. Some of the amendments of the Dodd-Frank Act include changes in capital requirements, executive compensation and corporate governance, the direction of the CFPB, the regulatory burdens on community banks (banks with less than \$10 billion in assets), stress testing,

mortgage foreclosure, loosening of lending standards, and the Bank Secrecy Act and Anti-Money Laundering laws.

The DFI is also watching the following issues over the next few years, as regulatory oversight continues to evolve and tighten:

- Fintech companies offering traditionally banking products.
- Effective regulation of Non-bank Financial Institutions and the impact on global economic conditions.

(3) Use of technology for education

The DFI used social media to provide free education to its licensees and consumers. This year, the DFI has focused training on cybersecurity for licensees, consumers, and examiners. The DFI frequently updates its website with regulatory guidance or training videos and sends “e-blasts” to affected industries. The DFI uses YouTube videos to educate licensees about regulatory compliance issues. Every year, the DFI uploads a training session to remind licensees about renewal requirements; this has increased compliance and reduced the processing time to renew licenses. The DFI has also used Twitter to quickly alert followers to new developments or information about fraud, elder financial abuse, cybersecurity, disaster planning, the DFI website updates, and upcoming training opportunities.

(4) Use of technology for applications

The DFI uses the Nationwide Multistate Licensing System (NMLS) to process applications for the non-depository industries of mortgage loan originators, mortgage loan originator companies, mortgage servicers, money transmitters, and escrow depository companies. This technology allows licensees to input information about their licenses in one place and that information is provided to all state regulators, thereby increasing efficiency for our licensees. This technology also requires licensees and applicants to respond to each question before submitting an application to the DFI for review. The DFI communicates with applicants through a secure email channel.

(5) Use of technology for examination requests

The DFI is using a secure email system to both send and receive examination request information from licensees. Use of this technology has eased the communication between the examiner and licensee and reduced the number of days the DFI spends on-site at any location.

(6) Business continuity/disaster planning

The Commissioner of Financial Institutions continues to participate with the financial institutions (all banks and credit unions) to improve communication and disaster planning. The DFI has continued to provide information to consumers about disaster recovery and how to plan and recover from a disaster.

(7) CSBS District V

The Commissioner of Financial Institutions serves as Chairperson for the CSBS District V, which consists of the commissioners for banking departments in the Western states of the U.S. As Chair, the Commissioner of Financial Institutions coordinates semi-annual meetings of the District V states and territories to discuss emerging issues in supervision, regulation, and examination, with

emphasis on issues affecting Alaska, Arizona, California, Guam, Hawaii, Idaho, Montana, Nevada, Oregon, Utah, and Washington. The meetings also include representatives of the FDIC, FRB, CFPB, and Office of the Comptroller of the Currency. The Commissioner of Financial Institutions also serves on several CSBS committees, including the regulatory compliance, supervision, technology, and legislation committees with other state commissioners.

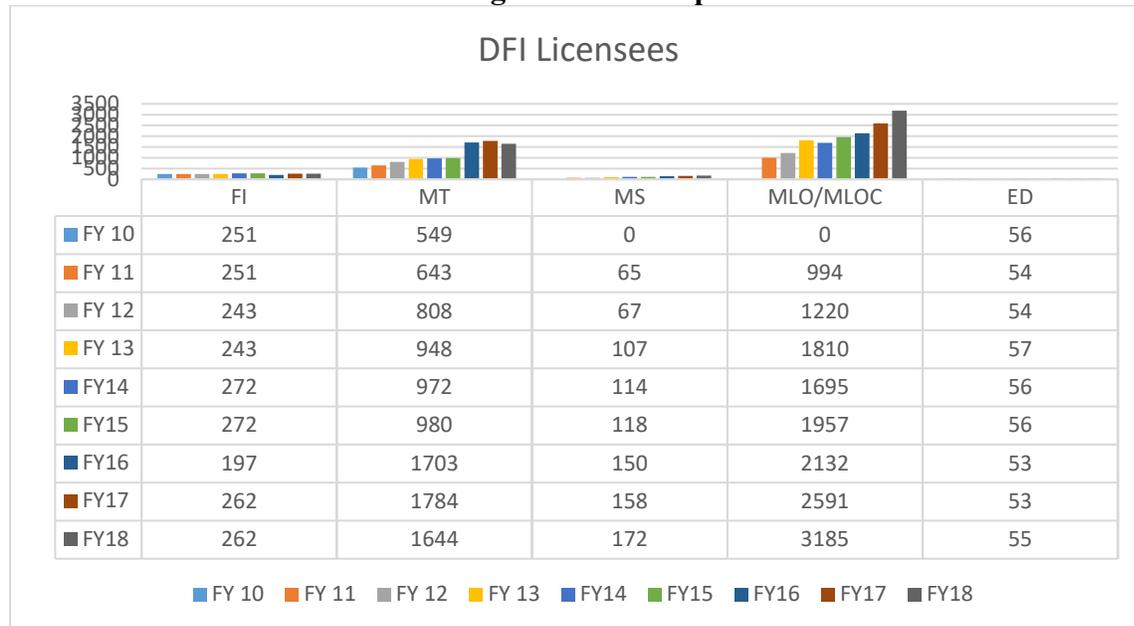
(8) Efficiency

The DFI continued its efforts to automate the initial application and renewal process for mortgage loan originators, mortgage loan originator companies, mortgage servicers, money transmitters, and escrow depository companies. The limited success of this automation is due to statutory constraints that will be addressed in upcoming legislative sessions. With automation, additional electronic tools are necessary to implement document management by chartered institutions and licensees. The automation effort includes filing additional documentation through the NMLS. All states can share regulatory information with one another to assist in ongoing supervision, licensing, and enforcement of multi-state licensees.

(9) Workload

The DFI’s workload has increased dramatically, both in the type and number of institutions regulated (*see* Chart 1: Number of Institutions Regulated and Supervised) and in the scope and complexity of the work.

Chart 1: Number of Institutions Regulated and Supervised



The complexity, security, and privacy of the money transmitter industry and emerging payments industry has increased exponentially. Money transmitter companies use the newest technologies and are innovative in how they transmit funds from person-to-person, business-to-business, and person-to-business. Following trends in other states, money transmitter companies are no longer “mom and pop” stores; instead, money transfers via virtual wallets and mobile devices, and the use of internet money transfers, prepaid cards, and virtual currencies has expanded in this rapidly

developing industry. The DFI is working to address these issues as they impact cybersecurity, consumer security and privacy, potential money laundering and fraud, and others.

The DFI has implemented its examination program for mortgage loan originator companies and mortgage servicers. With over 400 licensed companies that need to be examined at least once every five years, the DFI added additional examiners to properly examine these companies. In 2018, the DFI had six field examiners conducting examinations. To improve efficiency, the DFI has teamed with other states to conduct multi-state examinations on the larger mortgage loan originator companies and mortgage servicers. In addition, the DFI has teamed with the CFPB in examining very large (licensed in 35 states or more) mortgage loan originator companies and mortgage servicers.

CRF FINANCIAL SUMMARY

The following is the DFI's CRF financial summary for FY 2017-2018:

Personnel Expenses	Operating Expenses	Total Expenses	Revenues Received
\$3,657,485	\$573,996	\$4,231,480	\$5,678,123

CONCLUSION

The long-term impact of the global financial crisis of the last decade has created a “new normal” for financial service products and delivery of products and services. This evolution has increased supervisory oversight, as mandated by new federal laws and as a response to consumer expectations. New federal laws changing the requirements under the Dodd-Frank Act have added a new complexity to supervising both large banks and community banks.

The major outcome of the global financial crisis is fintech companies disrupting the financial industry by offering products and services traditionally offered by banks. Consequently, information security, cybersecurity risks, and data privacy have become a focus for the DFI. Training and finding staff in this area is challenging due to the disparate salaries offered by the DFI and private industry. The DFI continues to aggressively respond to these rapidly changing global and local economic conditions and pursues the active regulation and supervision of Hawaii-chartered financial institutions to preserve their safety and soundness and protect the rights of depositors, borrowers, consumers and other members of the community.

Overall, the DFI and its federal partners have provided Hawaii's state-chartered banks and financial institutions with the supervision necessary to operate in a safe and sound manner, with adequate capital and capable management. Oversight over non-depository financial institutions has increased due to their complex business models, innovative use of product delivery, and creative thinking to circumvent state and federal laws in providing products and services to consumers.

During FY 2018, while the DFI maintained its established regulatory, supervisory, and licensing programs and devoted considerable resources to implementing the newer mortgage servicer and mortgage loan originator examination programs, the division continued finding solutions to

overcome its resource challenges. Previous appropriations by the Legislature to increase DFI staffing will improve the division's ability to provide appropriate ongoing supervision, regulation, and examination of licensees for the protection of consumers. The DFI continues to use technology and social media to inform and educate licensees and consumers, process applications from applicants and licensees, and conduct examinations on licensees.

The mission and goals of the DFI have been met through its service to applicants, state-chartered institutions, state-licensed companies and individuals, and Hawaii's residents. The focus on cybersecurity, information security, and information technology will continue as companies use technology more innovatively and creatively. The DFI will endeavor to keep pace with the changing times through training opportunities and providing appropriate oversight over licensees.