LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR

STATE OF HAWAII
OFFICE OF THE DIRECTOR
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS
335 MERCHANT STREET, ROOM 310
P.O. Box 541
HONOLULU, HAWAII 96809
Phone Number: 586-2850
Fax Number: 586-2856
www.hawaii.gov/dcca

LAWRENCE M. REIFURTH
DIRECTOR

RONALD BOYER
DEPUTY DIRECTOR

TO THE HOUSE COMMITTEE ON FINANCE

THE TWENTY-FIFTH STATE LEGISLATURE
REGULAR SESSION OF 2009

Monday, March 2, 2009
12:30 p.m.

TESTIMONY ON H.B. NO. 1438, H.D.1 - RELATING TO MORTGAGE LOAN ORIGINATORS

THE HONORABLE MARCUS R. OSHIRO, CHAIR,
AND MEMBERS OF THE COMMITTEE:

My name is Nick Griffin, Commissioner of Financial Institutions ("Commissioner"), testifying on behalf of the Department of Commerce and Consumer Affairs ("Department"). We appreciate the opportunity to testify on House Bill No. 1438, H.D.1. The Department opposes the bill, and believes it to be unnecessary.

In each of the past five years, the Department has submitted (or, in one case, supported) legislative proposals to this committee that it believed would address problems in the mortgage broker industry and the Hawai'i housing market. We have worked steadily over that time to bring various industry and interest groups together to try to reach consensus on a revised approach to mortgage broker regulation. Consensus, however, proved elusive, and, as a result, legislation did not pass. This past summer, securitized mortgages (promoted largely by mortgage brokers) lost their value, and the United States housing and financial markets spiraled downward.

Mortgage brokers no longer play a central role in the nation's or Hawai'i's housing market. Residential real estate appears largely, once again, under the control of lenders, who define the market and effectively limit the operation of mortgage brokers. In addition, Congress has addressed the subject by enacting the *Secure and Fair Enforcement for Mortgage Licensing Act* (the "SAFE Act"), Public Law 110-289, Part V, which endorses the Nationwide Mortgage Licensing System (NMLS) for residential mortgage loan originators and provides important tools to establish a more robust nationwide mortgage broker (*aka* mortgage loan originator) regulatory and supervisory infrastructure.

The SAFE Act provides that, with few exceptions, everyone who performs mortgage loan originator functions should be licensed. The law also requires federal banking regulators to "register" mortgage loan originators that work for federally regulated depository institutions – e.g., banks, S&Ls etc. – which will provide the "even playing field" for which mortgage broker industry groups have been calling. If states do not implement laws consistent with the SAFE Act by federally established deadlines, mortgage loan originators in those states will fall under regulation to be provided by the federal Department of Housing and Urban Development ("HUD").

Although the Department previously advocated regulatory reform of the State's mortgage broker industry, a State sponsored initiative now is untimely, arguably irrelevant, and an inappropriate use of State funds in the midst of a significant economic slowdown.

The stated purpose of the bill is to allow the Commissioner of Financial Institutions to regulate, license, examine and enforce laws regulating mortgage brokers and loan originators, and to repeal Hawaii Revised Statutes ("HRS") Chapter 454, which presently governs the licensing of Mortgage Brokers and Solicitors. The Department opposes the bill for the following five reasons:

Relevance – The issues addressed by the proposal are no longer pressing. Lenders no longer offer the dangerous "sub-prime", "non-traditional", pay option, teaser rate mortgage loans which were the products that needed to be addressed. In addition, mortgage lenders are now extremely cautious about accepting mortgage loans brokered to them from the marketplace and, in most instances, utilize a very discreet number of specific, pre-screened, pre-qualified, and closely supervised mortgage loan originators (either employed or independently contracted) to provide loans for their mortgage pipe lines. The days of accepting brokered mortgage transactions from unvetted sources have ended for the foreseeable future.

Initial Funding Expense – Estimates show an initial cost of $470,000 to mobilize for program implementation (e.g., hire initial staff, conduct training, purchase furniture, fixtures and equipment, establish the requisite administrative infrastructure, etc.). That $470,000 does not include either the cost or the time required to join the Nationwide Mortgage Licensing System, both of which will be considerable, and may not run concurrently with the mobilization phase of program implementation. This bill entirely fails to address these and related program implementation costs, for which provision must be made. In addition, a SAFE Act compliant State program would be expensive for the significantly diminished number of active mortgage loan originators that would be regulated by such a program.

Staffing – In order to implement a SAFE Act compliant State statute, the Department would hire up to five new staff members in order to administer the program in accordance with federal standards. The new staff would be particularly specialized and outside recruitment would likely be needed to fill the majority of the positions. We estimate ongoing annual costs for these new staff members would be approximately $375,000.

Deadlines – Adopting a SAFE Act compliant State statute to address the issue would impose deadlines that can no longer be met. During the 2008 legislative session, the Department pointed out that, in order to ensure timely State compliance if Hawaii wished to adopt a State program to regulate its mortgage loan originators, it was critical to take immediate steps to enact a State-sponsored mortgage loan originator program that conformed to the federal SAFE Act, then soon to be passed. As the 2008 Session Administration bills failed to obtain passage, neither the initial federally mandated deadlines for compliance with the SAFE Act nor the extended federal deadlines potentially available to those states that can demonstrate that they are making a good faith effort to comply with the federal law, appear achievable.

Alternatives – Since the proposed measure clearly fails to make adequate provisions to establish a viable State mortgage loan originator regulatory and supervisory program that can comply with SAFE Act requirements within the timeframes permitted under federal law, under the provisions of the SAFE Act, a mortgage loan originator regulatory and supervisory program will automatically be established and administered for the State of Hawaii by HUD. The HUD federal mortgage loan originator regulatory and supervisory program will:

- end the protracted and essentially unproductive debates over what is or is not appropriate as far as a State mortgage broker statute is concerned;
- result in significant cost savings for the State, which already reportedly anticipates a budget shortfall of almost two billion dollars over the next several years; and

- provide a professionally staffed, up-and-running program that will immediately benefit both regulated mortgage loan originators as well as Hawaii's consumers.

The Department therefore recommends that your committees defer this unnecessary measure, allowing Hawaii's consumers, mortgage brokers and mortgage lenders to benefit from a professionally staffed, up-and-running federal regulatory and supervisory initiative, while at the same time saving Hawaii's taxpayers from initially funding a costly and potentially inadequate State administered program, which in the near term is arguably not needed to address problems that no longer exist in the marketplace and diverts critical funding from more productive uses in these troubled times.

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

OFFICE OF HAWAIIAN AFFAIRS
Legislative Testimony

HB 1438, HD 1 Relating to Mortgage Loan Originators
Committee on Finance

March 02, 2009 12:30 p.m.
Room 308

The Office of Hawaiian Affairs **supports** the purpose and intent of HB 1438 , HD 1.

Consumer protection laws benefit all of Hawaii's residents which include the beneficiaries of the Office of Hawaiian Affairs.

Mortgage Brokers and Loan Originators working with first time homebuyers need to be very unique individuals committed to doing more than expected for the benefit of the homebuyer. However, many are inexperienced and need laws to regulate their activities to the benefit of the homebuyer. The first time homebuyer is also inexperienced in the process of purchasing a home and these consumer protection laws benefit their education in this process as well.

We recognize that physical solutions by themselves will not solve social and economic problems, but neither can economic vitality, community stability, and environmental health be sustained without a coherent and supportive physical framework like these consumer protection laws.

Mahalo nui loa for the opportunity to provide this testimony and we urge your support.

(HBA) / **HAWAII BANKERS ASSOCIATION**

1000 BISHOP ST., SUITE 301B • HONOLULU, HAWAII 96813-4203
PHONE: (808) 524-5161 • FAX: (808) 521-4120

Presentation to the House Committee on Finance
Monday, March 2, 2009, at 12:30PM

Testimony for HB 1438 Relating to Mortgage Loan Originators

TO: The Honorable Marcus R. Oshiro, Chair
The Honorable Marilyn B. Lee, Vice Chair
Members of the House Committee on Finance

My name is Neal Okabayashi and I testify for the Hawaii Bankers Association in strong support of HB 1438. We believe that though the bill is a work in progress, it should be adopted without amendments (except for a defective date) so that the bill can be completed in conference.

Last year, in response to ample evidence of the role played by some mortgage brokers in the credit crisis, the United States adopted the SAFE Act which outlines the parameters states should use in creating a regulatory format to regulate individual mortgage brokers, now called mortgage loan originators. States were given until July 31, 2009 to adopt a state law regulating mortgage brokers which is compliant with the SAFE Act or be penalized by having HUD (Department of Housing and Urban Development) take over a state's regulatory oversight of loan originators. Loan originators would not save any money if HUD became their regulator, in fact, would likely pay more but they would pay the fees to HUD, not DCCA. If a state adopts a law that is compliant with the SAFE Act before July 31, 2009, it has two years to implement the state law. HUD decides if a state law complies with the SAFE Act and if not, HUD will take over.

To assist states, the Conference of State Bank Supervisors ("CSBS") and the American Association of Residential Mortgage Regulators drafted a model act which has been approved by HUD as compliant with the SAFE Act. This bill is based on the model act.

In essence, the SAFE Act requires all loan originators obtain a unique valid identifier (think of it as a social security number). Using the identifier, each state regulator must enter into a national registry the disciplinary history of an originator, and thus all other state regulators as well as the public can research the disciplinary history of an originator applying for a license or one that a person is about to do business with.

Employees of a bank, credit union, or one of their subsidiaries that is regulated by a federal banking agency, must obtain their unique identifier from their federal banking regulator.

While the existing chapter on mortgage brokers regulates individuals and companies, under the SAFE Act, only individuals have to be tested and licensed by a state.

There are critical issues to be addressed but it requires the cooperation of DCCA. DCCA is not funded by general funds but by fees paid by those who are regulated by DCCA. Thus, their input on application and license fees is critical. For now, either the fees are left blank or mirror the fees in last year's administration mortgage broker bill.

In last year's administration mortgage broker bill, DCCA requested an appropriation of $140,000 from the Compliance Resolution Fund for start up costs but in this bill, the amount is left blank since no input has been received from DCCA. See section 9.

In conference, we also need to amend section 8 on transitional matters. The State has until July 31, 2011 to implement the new law although the HUD envisions implementation by July 31, 2010 for those who presently do not have a license. Since we cannot have two regulatory frameworks on loan originators to exist side by side, at some point between the effective date and July 31, 2010, chapter 454 must be repealed but we cannot repeal it until the State is ready to license originators under the new law, otherwise, no one could become licensed as a loan originator. It may well be that next session may be a better time to decide on the repeal date of chapter 454 (or in the alternative, limit its reach only to companies) and also give us the time to make technical amendments as well as conforming changes in the law. However, the basic law, as set forth in this bill, must be passed this year.

The transitional provisions should also provide that presently licensed originators do not have to licensed until the time DCCA is able to test and license all candidates for a license.

However more time and input from DCCA is required to flesh this out and thus, our suggestion that these things be worked out in conference.

However, there is urgency for Hawaii to pass this law. Fannie Mae notified all lenders on that beginning January 1, 2010, on all mortgage loan applications, the unique identifier of the originator must be provided to Fannie Mae. Fannie Mae indicated they have some flexibility in that deadline but its letter verifies the importance of this legislation for the Hawaii.

I would like to address two requests for amendments which may be offered by other parties.

If HFSA asks for an exemption for employees of state regulated entities from section 16 and 17 of the bill, we strongly oppose it because it will likely make Hawaii's law non-compliant with the SAFE Act, is unfair to the other originators and is inconsistent with the consumer protection goals of the SAFE Act.

Section 17 is the section prohibiting fraudulent activity and basically is a: be honest, do not lie, cheat or steal provision. They are the heart of the anti-fraud provisions which are integral to one of the goals of the SAFE Act which is to promote consumer protection. These provisions include: (1) a prohibition on misleading and deceptive advertising (many of us are familiar with letters urging us to refinance a loan which appear to be from our existing lender), (2) a prohibition on door-to-door sales which was a problem in the Hamakua Plantation situation and requested by the ILWU and (3) a prohibition on filling in certain blanks (this is an outgrowth of complaints echoed by the Legal Aid Society and consumer advocates during a previous mortgage broker task force and legislative discussions). Why HFSA wants to exempt its employees from such honesty provisions is a mystery? It is not a burden to comply with an "act honestly" provision.

Exempting any individual who is by Congressional fiat to be subject to state regulation destroys one of the key precepts of the SAFE Act because one of the goals of the SAFE Act is to create a supervisory database and track originators. Among other powers, the commissioner has the power to revoke the license of an originator who violates the chapter including the anti-fraud provisions of section 17. But if an employee of an HFSA member is not subject to the anti-fraud provisions of section 17, then he can engage in fraudulent behavior and still not be in violation of the chapter and thus, the commissioner may not revoke his license for fraudulent activity. If the commissioner cannot pull the originator's license for dishonest behavior then we have lost the ultimate hammer to ensure that originators do not engage in practices which have contributed to the present credit crisis. It is the ultimate hammer because without a license, the originator may no longer be a loan originator and will be out of business. Further, the commissioner cannot file a report of the originator's fraudulent behavior to the nationwide mortgage licensing system and registry and thus other state regulators and consumers will not know about the fraudulent behavior of an originator simply because the originator happened to work for a state regulated entity.

It is not unusual for a mortgage broker whose license is revoked or is under some other regulatory discipline simply moves to another state and starts all over. As stated by the CSBS in testimony before Congress last March, the goal of the nationwide mortgage licensing system is to track individuals across state lines over any period of time and "consumers and the industry will eventually be able to check on the license status and history of companies and individuals with which they wish to do business." If employees of HFSA members are not subject to the anti-fraud protection provisions, we will undermine the goal of tracking miscreants because they can engage in fraudulent behavior without worry of discipline or having their disciplinary history entered into the nationwide mortgage licensing system so they can be tracked across state lines. Thus any proposed exemption of HFSA would would jeopardize Hawaii's compliance with the SAFE Act.

The actions of CSBS demonstrates this point. Recently, CSBS asked HUD for a greater clarification of SAFE Act and requested a reasonable delay in the licensing requirements for certain individuals on the basis that if states tried to address those situations through amendments to state legislation introduced to comply with SAFE, such states would risk being noncompliant with federal law. In other words, any attempt to amend the model act by creating exemptions from it endangers compliance with the SAFE Act. Similarly, the attempt by HFSA to exempt themselves from parts of this bill would also risk leaving Hawaii out-of-compliance with federal law and thus should be resisted.

It is unfair to loan originators to exempt a select class of originators from certain parts of the bill. It was not the intent of the Congress or CSBS to establish a caste system in the state regulatory framework. Congress did not exempt employees of state regulated entities from the SAFE Act. More importantly, the CSBS, which regulates state entities, did not exempt employees of state regulated entities from the prohibited practices provision of the model act.

It cannot be credibly argued that the anti-fraud provisions of section 17 to be honest are a burden on the employees of members of HFSA.

Reliance on state regulation of an entity that employs an originator would be misplaced. In a recent letter to Elizabeth Warren, chair of the Congressional Oversight Panel, John Dugan, the

Comptroller of the Currency that regulates national banks, said that there are "many, many federal consumer protection laws, rules and supervisory guidance applicable to national banks" and pointed out that "the overwhelming preponderance of toxic subprime mortgages were originated by companies subject only to state regulation." The OCC also conducted a study of ten areas with the highest foreclosure rates in the period 2005-2007, and of the 21 firms comprising the worst ten, 12 firms which accounted for nearly 60% of the non-prime mortgage loans and foreclosures were exclusively regulated by a state. The Comptroller went on to write "the market leaders for these products were nonbank brokers and lenders regulated exclusively by the states."

Those thoughts are in line with the words of the Treasury Department which issued a Blueprint for a Modernized Financial Regulatory Structure last March and said: "Federally regulated mortgage lenders and their employees are subject to an extensive scheme of federal supervision of their lending practices and compliance with applicable law and regulations." Therefore, the Treasury recommended "subjecting" originators who "are not employees of federally regulated depository institutions (or their subsidiaries) to uniform licensing qualification standards."

Even the CSBS recognized the gap in regulation. In testimony before Congress on March 4, 2008, a representative of CSBS testified that federal banking regulators had issued or proposed two guidances on nontraditional mortgage product risk and subprime lending which are not applicable to the many state lenders that they supervised, including no doubt members of HFSA, the CSBS tried to fill the gap by drafting sample parallel guidance which a state could issue with respect to the nondepository lenders that it supervised. In fact, federal banking regulatory guidances on subprime and predatory lending dates back to 1997.

One reason for the focus of the SAFE Act on non-federally regulated lenders was the recognition that the abuses in mortgage lending which eventually led to the SAFE Act was generally the acts of either non-regulated lenders or state regulated lenders.

A HUD-Treasury Report said: "However, there is a growing body of anecdotal evidence that an unscrupulous subset of those subprime actors – lenders (often those not subject to federal banking supervision), as well as mortgage brokers, realtors, and home improvement contractors – engage in abusive lending practices that strip borrowers' home equity and place them at increased risk of foreclosure."

In the Blueprint for a Modernized Financial Regulatory Structure, the Treasury Department wrote: "Mortgage market participants (both brokers and lenders) with no federal supervision have been responsible for a substantial portion of the mortgages and over 50 percent of the subprime mortgages originated in the United States. These mortgage market participants are subject to uneven degrees of state level oversight (and in some cases limited or no oversight)". The Treasury Department went on to write: "Brokers and lenders not subject to federal oversight have repeatedly been cited as the source of abusive subprime loans with adverse and profound consequences for consumers, the mortgage markets and the financial system as a whole."

It is clear that there is a vast difference between federal banking regulatory oversight and state regulatory oversight, and ultimately this question should be decided by the fact that exempting anyone from the anti-fraud provisions jeopardizes Hawaii's compliance with the SAFE Act.

Legal Aid may request that any loan made in the name of an unlicensed originator be declared void so the borrower who received the monies does not have to repay the loan. They apparently base their argument on the theory that by not punishing the unlicensed originator but punishing the innocent lender who ends up buying the loan somehow promotes consumer protection. They premise their argument on the Beneficial vs. Kida case.

This bill provides punishment to the originator for the originator's fraudulent activities. But nowhere in the model act and this bill does it suggest, as Legal Aid does, that the originator should remain unpunished for his fraudulent activity but the lender who did nothing more than provide the money for the loan or who later buys the loan should be punished.

Just because the originator happened to be unlicensed when the loan is made does not necessarily mean there was an act of consumer protection. The lack of license could be the result of a clerical error or administrative error such as not timely renewing a bond. More importantly, the innocent lender has no way of protecting itself because it cannot determine if the lender is licensed at 8:01 am on the recording and disbursement day of the loan.

The Kida case also poses the possibility of collusion between the borrower and the loan originator. For example, what if the borrower and the loan originator are romantically linked? The loan originator deliberately lets her license lapse and makes a loan to her boyfriend using the funds of the lender who will buy the loan. The boyfriend who received the loan proceeds can claim on the basis of the Kida case that he should not have to repay the loan. In fact, the facts of the Kida case are not far removed from my hypothetical as the unlicensed broker was the ex-girlfriend of the borrower.

Legal Aid should focus on punishing the originator instead of punishing the innocent lender and giving the borrower who received the loan proceeds a windfall.

In summary, HBA strongly supports this bill and urges its passage.

HAMB
HAWAII ASSOCIATION
OF MORTGAGE BROKERS

March 1, 2009

To: The Honorable Marcus R. Oshiro, Chair - Committee on Finance
The Honorable Marilyn B. Lee, Vice Chair - Committee on Finance
Members of the House Committee on Finance

Re: H.B. 1438 – Relating to Mortgage Loan Originators

I am Greg Ravelo, President of the Hawaii Association of Mortgage Brokers. The Hawaii Association of Mortgage Brokers (HAMB), a 200+ member organization, actively works to improve the mortgage broker industry since its charter in 1992.

We support passage of H.B. 1438

After the close of the 2008 Hawaii legislative session, the US Congress passed legislation known as the Title V – the SAFE Act, which when fully implemented will register all mortgage loan originators in the United Sates. It establishes a national registry of mortgage loan originators (MLOs) and will issue a permanent ID that will remain with individual MLOs through out their working careers. For MLOs not employed by government supervised depositories (e.g. Banks and S & Ls), the legislation requires background checks, pre-licensing education, testing and ongoing continuing education. This program will be will be administered by state regulators in most cases, however the federal Department of Housing and Urban Development (HUD) is required to implement the program in any state that does not adopt the federal program.

HB 1438 provides the legislative authority and direction to allow the Hawaii DCCA to modify the existing state program dealing with Mortgage Brokers (HRS Chap. 454) and expand it to include other covered MLOs while meeting the standards of the SAFE Act.

We understand that DCCA is opposed to operating the program based upon costs. They base costs upon a "from scratch" development rather than the costs to implement a set of federal standards. While it won't be easy, we believe that DCCA and industry representatives can, given sufficient time, come back to the legislature with a reasonable cost program that is acceptable to both groups.

We believe it is in the interest of the consumers of Hawaii to have the program operated by the state, rather than a federal agency.

Sincerely,

Greg Ravelo
President
808 748-8896

HAWAII FINANCIAL SERVICES ASSOCIATION

c/o Marvin S.C. Dang, Attorney-at-Law
P.O. Box 4109
Honolulu, Hawaii 96812-4109
Telephone No.: (808) 521-8521
Fax No.: (808) 521-8522

March 2, 2009

Representative Marcus R. Oshiro, Chair
and members of the House Committee on Finance
Hawaii State Capitol
Honolulu, Hawaii 96813

Re: **House Bill 1438, HD 1 (Mortgage Loan Originators)**
<u>Hearing Date/Time: Monday, March 2, 2009, 12:30 P.M.</u>

I am the attorney for the **Hawaii Financial Services Association** ("HFSA"). The HFSA is the trade association for Hawaii's financial services loan companies which are regulated by the Hawaii Commissioner of Financial Institutions under the Code of Financial Institutions (Chapter 412, Article 9 of the Hawaii Revised Statutes).

The HFSA **opposes this Bill as drafted.**

The purpose of this Bill is to allow the Commissioner of Financial Institutions to regulate, license, examine, and enforce laws regulating mortgage brokers and loan originators. This Bill repeals Chapter 454 of the Hawaii Revised Statutes ("HRS").

<u>Background:</u>

This Bill is an expansion of an effort that began a few years ago to regulate mortgage brokers. The most recent activity was during the 2008 legislative session with House Bill 2408, HD 1, SD 2 (Mortgage Brokers). Because of irreconcilable differences among the testifiers in 2008 regarding that 62 page mortgage broker bill, that bill did not move out of the Conference Committee.

After the 2008 Hawaii Legislative Session adjourned, Congress passed and President Bush later signed into law on July 30, 2008 the Housing and Economic Recovery Act of 2008 (Public Law 110-239). One component of that Act is the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 ("SAFE Act"). The SAFE Act establishes a uniform licensing and registration system for all loan originators, including mortgage brokers and loan officers. All loan originators at depository institutions will have to be <u>registered</u> (but not licensed) through the nationwide system. All other loan originators will be required to be <u>licensed</u> by a state or through a Housing and Urban Development ("HUD")-backup system if a state does not establish a licensing system.

Under the SAFE Act, a "loan originator" is an individual who for compensation or gain takes a residential mortgage loan application or offers or negotiates the terms of a residential mortgage loan. Loan originators fall into two categories:

1. One category is an individual who, simply stated, is an employee of a depository institution (such as a bank or a credit union). That individual is called a "registered loan originator" and will need to be <u>registered</u> with the Nationwide Mortgage Licensing System and Registry ("NMLSR").

2. The other category is an individual who is a loan originator but is not an employee of a depository institution. That individual will need to be <u>licensed</u> by a state or by HUD <u>and registered</u> with the NMLSR. This individual is called a "licensed loan originator". An example of a licensed loan originator is an individual who is a mortgage broker or mortgage solicitor. Mortgage brokers and solicitors are currently regulated in Hawaii under Chapter 454, Hawaii

Revised Statutes.

Another example of a "licensed loan originator" is an employee of a non-depository financial services loan company. Financial services loan companies are Hawaii financial institutions under the Code of Financial Institutions (HRS Chapter 412). Financial services loan companies make mortgage loans and personal loans just like other Hawaii financial institutions under HRS Chapter 412. It should be noted that HRS Chapter 454, relating to mortgage brokers, does not currently apply to employees of financial services loan companies which are exempt from HRS Chapter 454. However with the passage of the SAFE Act, an individual who is a loan originator and is an employee of a non-depository financial services loan company would be put in the same category as an individual who is a mortgage broker or mortgage solicitor. That individual would need to be licensed by the state or by HUD.

Within 12 months from the July 30, 2008 enactment of the SAFE Act, Hawaii and other states should develop licensing requirements to ensure applicants meet minimum standards including educational requirements, background checks, and testing. However, if a state does not establish a licensing system that meets the minimum requirements, HUD is directed to establish a licensing system for loan originators in the state.

In conjunction with the passage of the SAFE Act, two organizations of regulators, the Conference of State Bank Supervisors ("CSBS") and the American Association of Residential Mortgage Regulators ("AARMR"), prepared model legislation for states to consider enacting. Other groups such as the American Financial Services Association, of which the Hawaii Financial Services Association is a member, have proposed various amendments to the CSBS/AARMR model state legislation.

Because the SAFE Act was enacted after Hawaii's 2008 Legislative Session adjourned in May 2008, perhaps it's fortunate that the Legislature had the foresight not to pass the 2008 Hawaii mortgage broker bill. If that 2008 bill had become law, a substantial portion of it would have to be changed and rewritten during this 2009 legislative session.

How this Bill should be improved:

Much, but not all, of this Bill is identical to the CSBS/AARMR model state legislation. We support the provisions which are identical to the model legislation. But we have suggestions for improving this Bill:

1. There are some people within the banking community who are advocating the passage of this Bill as drafted even though bank employees who are mortgage loan originators would be totally exempt from this Bill under Sec. -2. On the other hand, non-depository financial services loan companies (the members of the Hawaii Financial Services Association) have a sincere and genuine interest in this Bill because they employ mortgage loan originators who would be covered by this Bill.

As stated above, non-depository financial services loan companies are Hawaii financial institutions under the Code of Financial Institutions (HRS Chapter 412). They make mortgage loans just like Hawaii banks and other financial institutions under HRS Chapter 412. Financial services loan companies are required to comply with certain capital requirements just like banks. They are regulated and examined by the Commissioner of Financial Institutions just like banks. And, just like banks, they are directly responsible and accountable for the actions of their employees, including any of their employees who are mortgage loan originators.

Under this Bill, the mortgage loan originators working for non-depository financial services loan companies are subject to the prohibited practices provisions in this Bill. Yet under this Bill, the mortgage loan originators working for state banks would not be subject to the same prohibited practices.

To protect Hawaii's consumers, all mortgage loan originators, whether or not employed by a bank or other depository institution, must be subject to the same prohibited practices listed in Sec. -17 beginning on page 32. Even if a bank's mortgage loan originator employee is to be exempt from the licensing and continuing education provisions of this Bill, to protect consumers, no mortgage loan originator should be exempt from the prohibited practices provisions. Prohibited practices must apply equally to the extent possible to all mortgage loan originators regardless of their employer.

The federal SAFE Act does not preempt or prohibit states from establishing prohibited practices that apply to **all** mortgage loan originators.

Here is how the Bill should be revised:

"**§ -2 Exemptions.** This chapter shall not apply to the following:

(1) A registered mortgage loan originator, when acting for an insured depository institution, a subsidiary of an insured depository institution regulated by a federal banking agency, or an institution regulated by the Farm Credit Association; provided that a registered mortgage loan originator employed by a financial institution as defined in chapter 412 shall comply with section -17 regarding prohibited practices;"

2. This Bill deviates from the CSBS/AARMR model state legislation by omitting certain provisions. However, one major deviation is for the prohibited practices. We believe that Sec. -17 beginning on page 32 of this Bill should be replaced completely with the 14 prohibitions in the model state legislation. And, to ensure that this Bill follows the model state legislation, there should not be any prohibitions other than the 14 prohibitions in the model legislation.

Here is how the Bill should be revised:

"**§ -17 Prohibited practices.** It shall be a violation of this chapter for a mortgage loan originator to:

(1) Directly or indirectly employ any scheme, device, or artifice to defraud or mislead borrowers or lenders or to defraud any person;

(2) Engage in any unfair or deceptive practice toward any person;

(3) Obtain property by fraud or misrepresentation;

(4) Solicit or enter into a contract with a borrower that provides in substance that the person or individual subject to this chapter may earn a fee or commission through "best efforts" to obtain a loan even though no loan is actually obtained for the borrower;

(5) Solicit, advertise, or enter into a contract for specific interest rates, points, or other financing terms unless the terms are actually available at the time of soliciting, advertising, or contracting;

(6) Conduct any business covered by this chapter without holding a valid license as required under this chapter, or assist or aide and abet any person in the conduct of business under this chapter without a valid license as required under this chapter;

(7) Fail to make disclosures as required by this chapter and any other applicable state or federal law including regulations thereunder;

(8) Fail to comply with this chapter or rules or regulations promulgated under this chapter, or fail to comply with any other state or federal law, including the rules and regulations thereunder, applicable to any business authorized or conducted under this chapter;

(9) Make, in any manner, any false or deceptive statement or representation including, with regard to the rates, points, or other financing terms or conditions for a residential mortgage loan, or engage in bait and switch advertising;

(10) Negligently make any false statement or knowingly and willfully make any omission of material fact in connection with any information or reports filed with a governmental agency or the Nationwide Mortgage Licensing System and Registry or in connection with any investigation conducted by the commissioner or another governmental agency;

(11) Make any payment, threat or promise, directly or indirectly, to any person for the purposes of influencing the independent judgment of the person in connection with a residential mortgage loan, or make any payment threat or promise, directly or indirectly, to any appraiser of a property, for the purposes of influencing the independent judgment of the appraiser with respect to the value of the property;

(12) Collect, charge, attempt to collect or charge or use or propose any agreement purporting to collect or charge any fee prohibited by this chapter;

(13) Cause or require a borrower to obtain property insurance coverage in an amount that exceeds the replacement cost of the improvements as established by the property insurer;

(14) Fail to truthfully account for monies belonging to a party to a residential mortgage loan transaction."

3. The written agreements provision in Sec. -16 beginning on page 29 is not in the CSBS/AARMR model state legislation. While two of the three provisions are in the existing mortgage broker law (HRS Chapter 454), a third provision is taken from last year's failed mortgage broker bill.

Sec. -16 beginning on page 29 should be deleted. In the alternative, your Committee should revise Sec. -16 (written agreements) to mirror HRS Sec. 454-3.1 (written agreements) of the existing mortgage broker law. Your Committee should delete provision (3), which is not in HRS Sec. 454-3.1, and reword provision (2). This way, Sec. -16 will be identical to the existing HRS Sec. 454-3.1. Nothing more. Nothing less.

4. HRS Chapter 454 regulates mortgage brokers and solicitors. Entities which act as mortgage brokers and which employ mortgage solicitors are licensed under HRS Chapter 454. Those entities, as employers of mortgage solicitors, are currently subject to all the requirements of HRS Chapter 454 including bonds, prohibited acts, and penalties.

However, Section 7 on page 50 would completely repeal HRS Chapter 454. As a result of this repeal, entities which are mortgage brokers and which employ mortgage loan originators (i.e. mortgage solicitors) would not be subject to any of the requirements in HRS Chapter 454 or any of the restrictions in this Bill. Under this Bill, these entities which are mortgage brokers and which employ mortgage loan originators would be unregulated.

Repealing HRS Chapter 454 is not be in the interest of consumer protection. For consumer protection purposes, there must continue to be a regulatory scheme for mortgage broker entities which employ mortgage loan originators. The federal SAFE Act does not preempt or prohibit states from regulating mortgage broker entities which employ mortgage loan originators.

HRS Chapter 454 should not be repealed. Section 7 on page 50 should be deleted.

This situation is different for employers which are financial institutions, such as financial services loan companies and banks, which employ mortgage loan originators. These financial institutions are exempt from HRS Chapter 454 and should continue to be exempt from HRS Chapter 454 because they are, and will continue to be, regulated under the Code of Financial Institutions which is in HRS Chapter 412. (But, as stated above, all mortgage loan originators who work for financial institutions should be subject to the prohibited practices in this Bill.)

Thank you for considering our testimony.

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

(MSCD/hfsa)