



LATE TESTIMONY

NEIL ABERCROMBIE
GOVERNOR

BRIAN SCHATZ
LT. GOVERNOR

STATE OF HAWAII
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KEALI'I S. LOPEZ
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TO THE
HOUSE COMMITTEE ON ECONOMIC REVITALIZATION & BUSINESS
THE TWENTY-SIXTH STATE LEGISLATURE
REGULAR SESSION OF 2012

Tuesday, January 24, 2012
8:30 a.m.

TESTIMONY ON H.B. 1840
RELATING TO STATE-OWNED BANK

TO THE HONORABLE ANGUS MCKELVEY, CHAIR, AND ISAAC CHOI, VICE CHAIR,
AND MEMBERS OF THE COMMITTEE:

My name is Iris Ikeda Catalani, Commissioner of Financial Institutions ("Commissioner"). I appreciate the opportunity to provide comments on behalf of the Division of Financial Institutions of the Department of Commerce and Consumer Affairs ("DFI") regarding House Bill No. 1840.

The purpose of the Bill is to establish a task force to study the feasibility of establishing a state-owned bank in Hawaii. It is believed that a state-owned bank would promote agriculture, education, community development, economic development,

housing and industry in the State by building a resource to help stabilize and grow the State's economy; use the resources of the people of the State within the State; support the common good and public benefit of the State; and leverage the State's financial capital and resources.

Members of the task force would be tasked with reviewing and evaluating the impact a state-owned bank might have on the State's economy. While I support the creation of the task force to explore the feasibility of a state-owned bank, in an effort to be proactive, DFI has already completed a white paper on the feasibility of a state bank. In doing so, we gathered information from the Bank of North Dakota, and the studies from the Federal Reserve Bank of Boston and the Massachusetts Commission created by the Massachusetts legislature. This white paper is attached at the end of my testimony.

As you are aware, only one state in the union has created a state-owned bank. In 1919 North Dakota established a state-owned bank primarily to help agricultural borrowers obtain financing needed to operate their businesses. While the Bank of North Dakota ("BND") facilitated financing for agricultural borrowers, there is no objective evidence that BND was instrumental in correcting severe credit shortfalls or that BND stabilized North Dakota's economy during the recent credit crisis. Indeed, there are extreme differences between North Dakota and Hawaii. Essentially, North Dakota's economy is supported by agricultural activities and populated by a small

number of isolated banks. Conversely, the Hawaiian economy is substantially supported by the tourist industry and governmental activities and has few and comparatively large banks, several of which have numerous branches throughout the State.

The cost of financing a state owned bank in North Dakota in 1919 was approximately 2 million dollars. When the state of Massachusetts recently considered opening a state-owned bank, start up costs were estimated to be approximately \$3.6 billion dollars. Arguably, establishing a state-owned bank in Hawaii might approach if not exceed the Massachusetts estimate given that both states are not agriculturally based, and that both state economies are driven by a complex mix of industries and businesses. Whether a state-owned bank can generate revenues to recoup start-up costs in addition to an annual operating budget, are factors which the task force should seriously consider in evaluating the viability of such a project.

There are well established programs in Hawaii, such as the Small Business Administration, which offer loans and financial assistance to small businesses. Until 2003, the state administered the Hawaii Capital Loan Program, which provided loans to eligible Hawaii businesses. During the 2011 session, S.B. No. 757 was introduced to reestablish the Hawaii Capitol Loan Program. Currently pending is a hearing to appropriate \$2 million dollars to the program.

Finally, and perhaps most importantly, are repercussions to the business community in the event the State establishes its own bank. I believe that a serious blow

may be dealt to the financial community if the State withdraws funds from local banks, and in turn, deposits State monies in a State-owned bank. The funds deposited by the State in our local banks are secured with bonds to ensure security and availability of the funds at all times. Arguably, the soundness of Hawaii's financial institutions may be compromised and jeopardized by transferring State monies to a state-owned bank.

As part of establishing the task force under the bill, I believe that it is important for the legislature provide the task force with guidance on the critical issues related to establishing a state bank such as:

1. What does the legislature want the state bank's mission or focus to be? The state bank of North Dakota was established to provide loans to farmers who were unable to qualify for agricultural loans in the 1900's. Its lending practices have not changed significantly since the establishment of the bank focusing on agricultural loans, and since 1967 adding student loans.

2. Whether the legislature wants the state bank to comply with the requirements that state funds deposited in banks be fully secured. Currently, all banks are required to maintain a minimum level of capital during the ongoing operations of the bank. In the alternative, whether the legislature wants to allow the state to float bonds to then invest as capital in the bank?

3. Where the capital to establish the state bank would come from and whether the state will put up the capital and be the 100% owner of the bank. The capital

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contribution would then not be considered state funds, but would be an investment of the state. Then if the state also required that all state funds (e.g. general funds, special funds, etc.) be deposited in the bank, then the question is whether the state will require that those funds be secured. In North Dakota, the original act of 1919 provided that all public funds were to be deposited with the Bank of North Dakota. An initiated measure in 1921 changed this by providing that all political subdivisions, with the exception of the state itself, make deposits either with private institutions or with the Bank of North Dakota.

4. Under what circumstances would the state bank be required to distribute dividends to the general funds. The State Bank of North Dakota did not provide a dividend to the state until 1945, about 26 years after the establishment of the bank.

Thank you for the opportunity to provide written comments and I am available to answer any questions the committee might have.

Should Hawaii Establish a State Bank?
By the Division of Financial Institutions
Iris Ikeda Catalani, Commissioner
January 2012

Department of Commerce and Consumer Affairs

With the recent economic downturn and lack of financing available for new businesses, discussions on the establishment of state banks have increased. The only state bank that currently exists was established in 1919 in North Dakota. Its primary functions are to promote agriculture, commerce and industry, and to stimulate economic development through several lending programs.¹

In May 2011, the New England Public Policy Center of the Federal Reserve Bank of Boston published a research report entitled, "The Bank of North Dakota: A model for Massachusetts and other states?" (Research Report). The Research Report analyzed the Bank of North Dakota (BND) as a possible model for the state of Massachusetts. The Report did not find this to be a reasonable model for Massachusetts, concluding that:

- The willingness and capacity of a state-owned bank to offset a serious credit crunch has not been shown;
- With the possible exception of the Great Depression, BND contributions to stabilizing the state economy and finances appear to have been relatively minor;
- The potential costs of starting up a state-owned bank could be significant; and
- Massachusetts and other states should start any discussions of financial-sector reforms by identifying the problems that public policy needs to address.

One of the factors the Research Report looked at was the difference in the banking environment in North Dakota which consists of numerous small commercial banks and that in Massachusetts which consists of a few comparatively large commercial banks. In addition, the Research Report noted that there is only one state bank in the entire country with no others with which to compare it.

¹ Morton, Heather. Are State-Owned Banks a Viable Option? NCSL LegisBrief November/December 2011.

While it is difficult to provide a definitive conclusion based on analyses which are limited and complex, the following provides additional discussion on why the establishment of a state bank in Hawaii would be against sound fiscal policy at this time.

- **Bank of North Dakota**

Emphasizing safe and sound lending, BND has a largely favorable reputation in the state. It does not engage in risky activities such as community development funding and equity investments. Partnering with small community banks in North Dakota allows these small banks to make loans that exceed their legal or internal lending limits. The experience of BND is not comparable to Hawaii economic or banking environment as the two states are dramatically different. North Dakota is sparsely populated rural state with an agricultural base with numerous small, relatively isolated banks,² differing significantly from Hawaii which relies on tourism, is not predominantly rural, and has only eleven banks, which could not be considered isolated.

- **Access to credit by local businesses.**

During the financial crisis and recession of 2007-2009, credit availability in North Dakota for small businesses was unable to meet the demand. There is no evidence that BND helped to lower credit barriers during that time. However, there is "indirect evidence that BND viewed federal agencies as having the primary responsibility and capacity for providing the liquidity backstop."³ While BND was able to assist North Dakota banks through "record loan growth, letters of credit for public deposits, and a record amount of fed funds borrowed," the Federal Home Loan Bank (FHLB) system was a major source of liquidity during this time. FHLB advances funding to various financial institutions to support small business when other sources of capital are scarce.

In addition, two new federal programs were initiated to aid small businesses. The Small Business Lending Fund and the State Small Business Credit Initiative both provide mechanisms to increase credit availability for small businesses. In addition, several loan guarantee programs of the Small Business Administration have been expanded and the Small Business Jobs Act of 2010 relaxed various SBA loan eligibility requirements.

- **Augmenting the lending capacity of local banks.**

² Kodrzycki, Yolanda K. and Tal Elmatad. New England Public Policy Center, Research Report 11-2, May 2011. The Bank of North Dakota: A model for Massachusetts and other states?

³ Ibid

While a state bank and BND in particular are able to augment local banks' lending capacities, Hawaii's banking industry does not mirror that of the small banks in North Dakota. Even if it did, the Massachusetts Commission Report pointed to "private bankers' banks" owned by and providing services to member institutions as an alternative model to a state bank. This model could provide services to smaller banks while not being viewed as a competitor of larger banks.

- **Stabilization of state economy and finances.**

When the North Dakota economy is doing well, BND has been able to help balance the state budget when it experiences shortfalls in other financial sources. However, during a severe agricultural crisis and recession, the poor performance of BND made the crisis worse. When North Dakota's economic experience was compared to that of South Dakota, a state similar in geographic location, size, population, and industry mix, it was found that North Dakota did not consistently outperform South Dakota. The conclusion of the Research Report, reflected in the Massachusetts Commission Report, is that having a state bank did not measurably affect the economic health of the North Dakota.

- **Start-up costs and considerations.**

In addition to the cost of possible legal and regulatory hurdles, including the time delays, basic start-up costs would probably be considerable, involving a sizeable bond issue. In addition, if a state bank were to be established quickly, it would most likely disrupt the operations of existing banks. This is because the state deposits state funds into various financial institutions and withdrawal of such deposits would be disruptive, requiring these institutions to reduce their lending and investment portfolios. However, a gradual phase-in, while perhaps more palatable to existing banks, would delay the benefits of state-owned bank lending. The Massachusetts study estimated that, based on the startup costs for BND which consisted of an initial capitalization through a \$2 million bond issue in 1919, the startup cost for a Bank of Massachusetts today would be around \$3.6 billion. This extrapolation included adjustments for inflation and for growth in the size of the economy from 1919 to today - assuming a 13-fold expansion.

- **Review of public policy issues.**

The Research Report recommended that, instead of planning for the establishment of a state bank, the Commission:

- Identify the specific market failure it wishes to address and the degree to which a state-owned bank would address this failure; and

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- Investigate ways to leverage the already existing network of quasi-public agencies to fulfill its objectives.⁴
- **Massachusetts state programs**
Many public and quasi-public agencies and nonprofits already exist in Massachusetts that offer "various lending programs and services, including lending to help support infrastructure."⁵
- **Hawaii state programs**
As in Massachusetts, a number of programs already exist to provide funding for various small businesses, etc. In addition, once the objectives for the creation of a state bank have been established, based on specific market failures, existing programs can be reevaluated and revised and new programs can be created, following the examples of other states.

Some of the programs already in existence in Hawaii include:

- Small Business
 - The federal Small Business Association in Hawaii offers services including helping small businesses find financing through loans, grants, and a variety of other methods, helping the business decide which method is best for each individual business. It does not provide loans but can help in filling out loan applications and provides numerous other services.⁶ The Hawaii banks provide the SBA loans to the small businesses.⁷
 - The Department of Business Development and Tourism (DBEDT) has developed a number of resources on how to start and grow a business⁸ and how to find financing.⁹ In addition to the small business resources above, the sources of financing on the DBEDT website include commercial lenders, Hawaii Strategic Development Corporation venture capital, Small Business Innovation Grants, OHA business loans, and agricultural loan programs.

⁴ Report of the Commission to Study the Feasibility of Establishing a Bank Owned by the Commonwealth; August 8, 2011.

⁵ Ibid

⁶ <http://www.sba.gov/about-offices-content/2/3112>

⁷ Hawaii banks that provide SBA loans are: American Savings Bank, Bank of Hawaii, Central Pacific Bank, First Hawaiian Bank, Hawaii National Bank, Ohana Pacific Bank, and Pacific Rim Bank.

⁸ http://hawaii.gov/dbedt/business/start_grow/

⁹ http://hawaii.gov/dbedt/business/find_financing/

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- o Hawaii Capital Loan Program

In 1963, the Hawaii Capital Loan Revolving Fund was created within the Hawaii Capital Loan Program (Program) to provide a variety of loans to aid certain businesses. In 2003, based on the downturn in the economy, the Fund was repealed as one of the funds which, according to Act 178, Session Laws of Hawaii 2003, no longer served the purpose for which it was created, was not an appropriate means of financing, or was not financially self-sustaining. According to DBEDT, in its 40 plus years of existence, the Program has assisted 561 borrowers providing financing of over \$96 million. Seventy-six loans were written off during that time totaling just under \$7.5 million.

In 2011, Senate Bill Number 757 (SB757) was introduced to appropriate funds for the Program. SB757 was amended to reestablish the Fund authorizing DBEDT to contract for servicing or administering loans from the Fund. The bill passed the Senate as SB757, Senate Draft 2, and passed out of the House Committee on Economic Revitalization and Business as SB757, House Draft 1. It has been referred to the Finance Committee. According to the committee reports for these two drafts, the only differences in the Senate and House versions are the effective dates, which were amended in both drafts to encourage further discussion. Neither bill provided the amount of the appropriation that would be attached to the Fund. However, House Bill 873 (HB873), also introduced in the 2011 session, reestablished the Fund and provided an appropriation of \$2,000,000. HB873 has not received a hearing.

Reestablishing this Fund would provide additional financial resources to small businesses that might otherwise be unable to find funding due to the recent downturn in the economy. Because the bill has passed the Senate and is in the final House committee, this could be accomplished reasonably quickly providing quick relief for small businesses that lack funding.

Finally, in 2010, the Massachusetts legislature passed legislation for a commission to study the establishment of a state bank. In August 2011, after six meetings and three public hearings, and considering many of the factors outlined above, the commission recommended against a state bank for Massachusetts because:

- There was no justification found for the initial capital costs;
- The BND did not offer adequate guidance because of the "vast" differences in the North Dakota and Massachusetts banking industries and economies;

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- Public funds deposited into a state bank would be exposed to an unacceptably high risk when used for risky gap financing;
- Massachusetts infrastructure investment is substantially more established than that of North Dakota; and
- Massachusetts already has a network of public agencies, quasi-public agencies, and non-profits which offer lending programs and services.

Conclusion

Whether a state bank should be created in Hawaii needs careful consideration prior to outlining how this would be accomplished. Of the many factors to consider, the determination of what the state bank would accomplish for the state is critical. Once these factors are outlined, perhaps another avenue of financial assistance could be found that would better accomplish the state's goal. Only once it is clear that a state bank is necessary and is the best method to accomplish one or more of these goals should the concept of a state bank be fully discussed and methods to create it are worked out. In addition, the drawbacks of the establishment of a state bank must be thoroughly discussed and solutions to those found unless they are an acceptable cost of the creation of the state bank.

Appendix A

	Hawaii	North Dakota
Economic Driver	Tourism	Agriculture, oil
Population	1,360,301 in 2010 - quadruple that of N.D. when the Bank of N.D. was established and over twice the current N.D. population	approx. 673,000 in 2010 - Just over 300,000 when the state bank was established
Number of banks	12 with 175 branches	95 banks with 442 branches http://www.moneyaisle.com/bank-browser/states/north-dakota/
Cost of start up	undetermined	\$325 million (estimated startup cost in today's dollars)
Community classification	Urban	Rural
Size in square miles	6,459	70,704
Unemployment rates ¹⁰	12 th (6.5%) ¹¹	1 st (3.4%) ¹²
Mortgage foreclosure rate ¹³	14th	49th
Nearest neighboring state	California - 2500 miles across the Pacific	South Dakota, Montana, Minnesota (on the border)
Climate	Warm, balmy	Cold

¹⁰ U.S. Department of Labor, Bureau of Labor Statistics

¹¹ Same for November 2011

¹² Same for November 2011

¹³ RealtyTrac, 2008 third quarter.

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Testimony of Paul A. Komara, Jr.
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January 23, 2012
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Were as effective 1/21/12, Timothy Durden, reported in the zerohedge.com/news/india-joins-asian-dollar-exclusion-zone

“For anyone wondering how the abandonment of the dollar reserve status would look like we have a Hollow Men reference: not with a bang, but a whimper...or in this case a whole series of bilateral agreements that quietly seeks to remove the US currency as an intermediate. Such as these: “ Worlds Second (China) and Third largest (Japan) economies to by pass Dollar, Engage in Direct Currency Trade”, “China, Russia, Drop Dollar In Bilateral Trade”, “China and Iran To Bypass Dollar, Plan Oil Barter System”, “India and Japan sign new \$15bn currency swap agreement”, and now this: “Iran, Russia Replace Dollar With Rial, Rubie In Trade, Fars Says.” “Today we add the latest country to join the Asian dollar exclusion zone: “India and Iran have agreed to settle some of their \$12 billion annual oil trade in rupees, a government source said on Friday, resorting to the restricted currency after more than a year of payment problems in the face of fresh, tougher U.S. Sanctions. “To summarize: Japan, China, Russia, India, and Iran: the countries which together account for the bulk of the world's productivity and combined are among the biggest explorers and producers of energy. And now they all have partial bilateral arrangements, and all of which will very likely expand their bilateral arrangements to multilateral, courtesy of Obama's foreign relations stance which by pushing the countries into a corner has forced them to find alternative, USD-exclusive, arrangements. But yes, aside from all of the above, the dollar still is the reserve currency...if only in which to make calculations of how many imaginary money one pays in exchange for imaginary 'developed world' collateral.

On India's induction into the dollar unluck club, from Reuters.

As a member of the Occupy Kona movement, a non-partisan movement, in solidarity with Occupy Wall Street, I present the latest world news about our Asian-Pacific trading partners. I did read on the internet about this after the Asian-Pacific meeting on Oahu in November, 2011.

It appears that the State of Hawaii has no choice but to protect itself. The Bank of North Dakota is the model bank of choice since it has accumulated State wealth during this world financial crisis. The State Bank of Hawaii must be able to exchange our Asian-Pacific partners currency without loss.

I further suggest that the Committee review the published works of Mr. David Wilcock, entitled, FINANCIAL TYRANNY: Defeating the Greatest Cover-Up of All Time, January 13, 2012. This factual documentation can be found at <http://www.divinecosmos.com> The documentation suggest that the above agreements between our Asian-Pacific trading partners are in place.

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**LATE
TESTIMONY**

Sherrian Witt, M.A., L.M.H.C.
P.O. box 917
Pahala, HI 96777-0917
808-928-8138

January 23, 2012

This letter is in support of legislation for a Bank for the State of Hawaii. It is apparent the financial condition of the banking industry of this country continues to victimize citizens with, in my opinion, unethical activity. A State Bank would boost our economy and create jobs and keep Hawaii from the vulnerable practices of "for-profit banks". Money for business enterprise should be regulated and controlled by the **citizens** of this state. As a citizen of the state of Hawaii I want my money to benefit my community. Keep the corporate raiders out of Hawaii.

Respectfully,
Sherrian Witt

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From: mailinglist@capitol.hawaii.gov
Sent: Monday, January 23, 2012 6:26 PM
To: ERBtestimony
Cc: sarawitt12@gmail.com
Subject: LATE TESTIMONY - Testimony for HB1840 on 1/24/2012 8:30:00 AM

Testimony for ERB 1/24/2012 8:30:00 AM HB1840

Conference room: 312
Testifier position: Support
Testifier will be present: No
Submitted by: Sherrian Witt
Organization: Individual
E-mail: sarawitt12@gmail.com
Submitted on: 1/23/2012

Comments:

From: mailinglist@capitol.hawaii.gov
Sent: Monday, January 23, 2012 7:47 PM
To: ERBtestimony
Cc: sandrascar@aol.com
Subject: LATE TESTIMONY - Testimony for HB1840 on 1/24/2012 8:30:00 AM

Testimony for ERB 1/24/2012 8:30:00 AM HB1840

Conference room: 312
Testifier position: Support
Testifier will be present: No
Submitted by: Sandra Scarr
Organization: Individual
E-mail: sandrascar@aol.com
Submitted on: 1/23/2012

Comments:

I read the Testimony of of Sam Munger, Director of the Center for State Innovation at the University of Wisconsin - Madison. He presented an economic analysis of the costs and benefits of the State Bank of North Dakota, which has been in existence for 90 years, and a proposed state bank in Washington state. I also read the Testimony of the Public Banking Institute, Imua Alliance, and Faith Action for Community Equity -- all of which support the formation of a Hawaii State Bank. I hope that the Hawaii Legislature will pass HB 1840 to enable a study of the costs and benefits of such a state bank.

From: mailinglist@capitol.hawaii.gov
Sent: Monday, January 23, 2012 9:41 PM
To: ERBtestimony
Cc: jbmkona@gmail.com
Subject: LATE TESTIMONY - Testimony for HB1840 on 1/24/2012 8:30:00 AM

Testimony for ERB 1/24/2012 8:30:00 AM HB1840

Conference room: 312
Testifier position: Support
Testifier will be present: No
Submitted by: Jean Bevanmarquez
Organization: Individual
E-mail: jbmkona@gmail.com
Submitted on: 1/23/2012

Comments:

My husband, Kawika Marquez, and I are in support of a state bank for Hawai'i. It is necessary for local businesses and community organizations to have access to resources for expansion of services and product lines to grow our economy. Banks have interests in making profits for share holders; state banks return those profits back to the community, it's collective owners. Let's take our recovery in our own hands, and return profits to our growth.

