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TO THE  
HOUSE COMMITTEE ON  
FINANCE

THE TWENTY-SEVENTH STATE LEGISLATURE  
REGULAR SESSION OF 2013

Monday, April 1, 2013  
2:00 p.m.

TESTIMONY ON S.B. NO. 1068, S.D. 2, H.D. 1  
RELATING TO MONEY TRANSMITTERS

THE HONORABLE SYLVIA LUKE, CHAIR,  
AND MEMBERS OF THE COMMITTEE:

My name is Iris Ikeda Catalani, Commissioner of Financial Institutions ("Commissioner"), testifying on behalf of the Department of Commerce and Consumer Affairs ("DCCA") in strong support of administration bill, Senate Bill No. 1068, S.D. 2, H.D. 1.

The Money Transmitter Act, Chapter 489D, was passed in 2006, and licensure of money transmitters has been required since July 1, 2007. The purpose of the law is "to

establish within the State a licensure system to ensure the safe and sound operation of money transmission businesses, to ensure that these businesses are not used for criminal purposes, to promote confidence in the State's financial system, and to protect the public interest.”<sup>1</sup> Legislative history indicates that industry regulation was necessary to prevent: (1) the laundering<sup>2</sup> of profits of illegal activities such as drug distribution, gambling, and prostitution; (2) consumer losses from fraud and unsound business practices related to wiring money to a location outside the State; and (3) illegal activities related to terrorism that utilize money transmission<sup>3</sup>. Prior to enactment of Chapter 489D, Hawaii was one of only five states that did not regulate money transmitters.

#### **Hawaii Statistics from 2012 Renewals by 35 Money Transmitter Licensees**

In 2012, after just five years of licensure, the 35 Hawaii licensed money transmitters and their delegates<sup>4</sup> transmitted **\$2.3 billion** for their customers, in some 9.6 million money transactions.

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<sup>1</sup> HRS sec. 489D-2.

<sup>2</sup> By “laundering money,” a money transmitter can make illegally-gained proceeds appear legal. This typically involves a three-step operation. First, the illegitimate funds are furtively introduced into the legitimate financial system. Then, the money is moved around to create confusion, sometimes by wiring or transferring through numerous accounts. Finally, it is integrated into the financial system through additional transactions until the “dirty money” appears “clean.”

<sup>3</sup> Senate S. Rep. No. 2904 (2006).

<sup>4</sup> “Authorized delegate” means an entity designated by the licensee under this chapter to sell or issue payment instruments or engage in the business of transmitting money on behalf of a licensee. HRS § 489D-4.

- This is the reason for DFI’s careful supervision of the industry, whether a money transmitter has a corporate location or works out of a “mom and pop” neighborhood store.
- This large volume was attained with an average transmission size of just \$241. The relatively small amount per average transmission cannot be overlooked. Sadly, funds that helped to finance the attacks on the World Trade Center were moved by money transmissions of \$2,000 over a one-month period.
- The security device amount required of a Hawaii-licensed money transmitter is very low, currently just \$1,000. At this level, in the event a money transmitter failed to send the money as requested, only four transmissions of “average” size would be covered.

<b>HAWAII LICENSED MONEY TRANSMITTERS (“MT”) (Source: 2012 License Renewal Data)</b>	
<b>All MT Licensees</b>	
Number of licensed MTs	35
Number of delegates	913
Dollar volume of money transmissions	\$2,328,380,367
Number of MT transmissions reported	9,679,372
Dollar volume divided by #of MTs	\$241 each transaction
<b>Hawaii Based Licensees Only</b>	
Number of licensed MTs	3
Number of delegates	33
Number of MT transmissions reported	133,540
<b>Off-Shore Based Licensees Only</b>	
Number of licensed MTs	32

Number delegates	910
Number of MT transmissions reported	9,545,832

NOTE: 45 licensed money transmitters as of 3/01/13.

### **Reason for Change of Renewal Fee Calculation**

The bill changes the annual renewal fee for money transmitters from a flat fee of \$2,000 plus \$300 per delegate, to a scaled fee schedule based on the number of money transmissions.

- The reason for the change in the annual fees is to create parity and recognize that large and complex companies who transmit more money for consumers pose a higher risk and will take additional time to supervise and regulate.
- This results in companies with more money transmissions paying more than those with a small number of money transmissions.

Under the fee schedule in the H.D. 1:

- Typically, the higher fees will be paid by internet and off-shore companies which have many delegates. The fee is capped at \$20,000.
- The small companies that transmit 5,000 or fewer money transmissions will see their fee drop from \$5,000 to \$3,000.
- For the “average” transmission size of \$241, this is just a 10 cent difference per transmission.

- The large companies with more than 200,000 transmissions will see an increase in their annual of fee to \$20,000 (up from \$15,000). These large companies are currently paying \$15,000 because they have a large number of delegates.
- The internet companies will see the largest adjustment in fees. These companies typically pay \$2,000 and we expect that these companies will pay anywhere from \$8,000-\$20,000 depending on the number of money transmissions.
- **There is no additional fee on a licensee for using delegates to conduct its business. A licensee can expand its business by adding more delegates, and there will not be a “per delegate” fee.**

To illustrate, here is an example of licensee fees under current law, as compared to fees under the H.D. 1 schedule:

<b>MONEY TRANSMITTER LICENSE RENEWAL FEE</b>		
	<b>Current fee paid</b>	<b>Proposed fee HD1</b>
<b>Hawaii MT company (each has one or more delegates)</b>	<b>\$5,000 (\$2,000 + \$3000 for 10 delegates).</b>	<b>\$3,000 based on the number of money transmissions</b>
Large off-shore MT company with delegates	\$15,000 (max) (\$2,000 + \$15,000 for 50 delegates)	\$20,000 (max)
Internet MT company with no delegates	\$2,000	\$8,000 to \$20,000

DFI anticipates that it will collect approximately \$279,000 in annual fees, based on the current number of licensees. DFI currently collects \$178,900 from its licensees.

**Self-Funding Requirement Necessitates Requested Fee Changes**

DCCA has been financially self-sufficient since 1999. Its operations are not funded by the Legislature's general fund, but instead by the persons and entities who are regulated by DCCA or who receive services from the Department. All funds for DFI are from the licensees (financial institutions, money transmitters, mortgage servicers, mortgage loan originators, mortgage loan originator companies, and escrow depositories), and fees that DFI may collect are set by legislation. **Since 2006, the Division has been given three new programs which do not collect adequate revenue to appropriately supervise those programs.**

DFI runs its operations like a business -- we do not spend more money than we generate. Like a business, we try to stretch every dollar by not hiring staff, which is an added expense. With an increased workload but without a commensurate increase in fees --

- The Division has refrained from filling its six staff vacancies as we do not have sustained funds to retain these positions for more than 1.5 fiscal years.
- The Division has a current 120 to 180 day backlog in processing licensing work, which is contrary to the best interests of consumers and business because:
  - It means delays in opening of new businesses and their hiring of employees which would contribute to the State's economy.

- It means delays in issuing license renewals rendering licensees with expired licenses unable to lawfully conduct business.
- We have not been able to fully examine our licensees which handle billions of dollars of consumer financial transactions annually, delaying the discovery of licensees who could benefit from the Division’s assistance and monitoring to help them restore their financial viability and strength.
  - Delays can potentially mean that questionable licensee conduct goes undiscovered in time to avert massive financial harm to the public.

**Money Transmitter Program Cost and Revenue**

The cost of operating the money transmitter program, and the fees that the program generates, are follows:

<b>MONEY TRANSMITTERS PROGRAM</b>					
	(A) DFI Total Salaries only	(B) % DFI Hrs (Money Transmitters Program)	(C) Cost of DFI Program Oversight [(A) x (B)]	(D) Program Revenue	(E) Program Shortfall or Net Revenue [(C) – (D)]
FY11	3,006,970	9.3%	279,648	212,973	(66,675)
FY12	2,999,126	9.6%	287,916	306,857	18,941
FY11-12					(\$47,734)

Revenue generated by the money transmitter program has exceeded DFI program costs by \$47,734 over the past two fiscal years.

**Advantages and Disadvantages of Using NMLS**

The bill authorizes the Commissioner to require money transmitters to register with the NMLS, a system for state licensing and registration of state-licensed financial services providers.

- The Division believes using NMLS will provide a cost-effective way for licensees to manage all of its State money transmitter licenses and will allow the Division to use the electronic method to review, oversee and license money transmitters.
- The Division must continue to ask for items outside NMLS for the state specific items required by our Hawaii law.
- The Division currently uses the NMLS<sup>5</sup> to manage mortgage loan originator licensees.

#### **Reason for Changing the Security Device or Bond**

The bill also adjusts the security device requirements for money transmitters. The security device is generally a bond (like insurance) that DFI holds for the benefit of consumers who have been harmed by a licensee or claim that the recipient had not received the funds transferred. As stated above, there is a requirement of a security device in the amount of \$1,000, which seems insufficient.

- The industry transmits over \$2.3 billion of customer money in Hawaii annually. If a money transmitter were to fail, the current \$1,000 security device would cover the claims of four customer transmissions of the “average” amount of \$241. The



increased security device amount proposed by this bill would increase the likelihood that more consumers could recover some money lost to a failed money transmitter.

- New money transmitter licensees have been voluntarily providing DFI bonds of \$10,000, as that amount is required by most of other states.

### **Requested Technical Amendment**

It appears that the citation to H.R.S section 346-97 on p. 28, line 14 of S.D. 2, should actually be to section 321-496, as referenced in S.B. 1068. It is requested that this correction be made to the bill.

**DFI strongly supports this administration bill, Senate Bill No. 1068, S.D. 2, H.D. 1 with the amendment recommended above.**

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

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<sup>5</sup> Formerly known as the “Nationwide Mortgage Licensing System,” the system changed its name to “NMLS” as it expanded its services beyond mortgage loan originator licensing, and can be used by non-depository institutions.