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Testimony of the Department of Commerce and Consumer Affairs

**Before the
House Committee on Intrastate Commerce
Tuesday, February 4, 2020
9:30 a.m.
State Capitol, Conference Room 430**

**On the following measure:
H.B. 2628, RELATING TO A BANK OF THE STATE OF HAWAII**

Chair Ohno and Members of the Committee:

My name is Iris Ikeda, and I am the Commissioner of the Department of Commerce and Consumer Affairs' (Department) Division of Financial Institutions (DFI). The Department offers comments on this bill.

The purposes of this bill are to: (1) direct the Department to conduct a comprehensive review of relevant state laws to develop legislation to establish a state-operated bank of the State of Hawaii; and (2) appropriate funds to conduct the review.

In 2012, the DFI issued a white paper entitled "Should Hawaii Establish a State Bank?".¹ The white paper considered various factors, including:

- (1) The Bank of North Dakota;
- (2) The Federal Reserve Bank of Massachusetts research report;
- (3) Access to credit by local businesses;

¹ This white paper is available at: <http://cca.hawaii.gov/dfi/learn-more-banks/>.

- (4) The lending capacity of local banks;
- (5) Stabilization of the state economy and finances;
- (6) Start-up costs; and
- (7) Public policy issues.

To establish a state-operated bank, the State must consider several factors. Managerial factors include the competence, experience, integrity, and financial ability of the bank organizers and management. Financial factors include the viability of the business plan and the ability to maintain profitability. Further, capital of approximately \$20 million is needed to address current funding and future growth and earnings.

Notably, the Bank of North Dakota is the only state-operated bank in the United States and was established due to the lack of credit available to farmers. In 1919, farmers in North Dakota were unable to obtain loans for farm equipment or loans to expand their agricultural acreage. Today, the Bank of North Dakota continues to act as a correspondent bank and has expanded its loan portfolio to include student loans.

The DFI's white paper concluded that the State must first determine what a state-operated bank would accomplish and be used for before it can analyze the managerial factors, financial factors, and capital requirements involved in establishing this financial institution.

Thank you for the opportunity to testify on this bill.



House Committee on Intrastate Commerce
Tuesday, February 4, 2020, 9:30 am
Hawaii State Capitol, Room 430

In Opposition to HB 2628, Relating to a Bank of the State of Hawaii

To: The Honorable Takashi Ohno, Chair
The Honorable Dale Kobasyahi, Vice-Chair
Members of the Committee

My name is Stefanie Sakamoto, and I am testifying on behalf of the Hawaii Credit Union League, the local trade association for 51 Hawaii credit unions, representing over 800,000 credit union members across the state. We offer the following testimony in opposition to HB 2628, Relating to a Bank of the State of Hawaii.

HB 2628 requires a comprehensive review of financial institution law be conducted by several state agencies, and to explore the feasibility of a state-operated bank of the State of Hawaii.

Our main concern is simply that funds being deposited into a state bank would be insured by the state itself. Without the benefit of being insured by a separate entity like the National Credit Union Administration (which insures and oversees all credit unions in the State of Hawaii), the state would be in an extremely precarious situation in the event of any financial difficulty within the bank, and within the state.

Thank you for the opportunity to provide comments on this issue.

Presentation to The
Committee on Intrastate Commerce
February 4, 2020 9:30 A.M.
State Capitol Conference Room 430

Testimony in Opposition to HB 2628

TO: The Honorable Takashi Ohno, Chair
The Honorable Dale T. Kobayashi, Vice Chair
Members of the Committee

My name is Neal K. Okabayashi, the Executive Director of the Hawaii Bankers Association (HBA). HBA is the trade association representing eight Hawaii banks and two banks from the continent with branches in Hawaii.

HBA opposes the idea of establishing a state bank after a study made by various state departments and agencies with the goal of developing legislation for a state bank.

Banks accept deposits, which are then used to write checks to obligors and make loans to borrowers with the ability repay the loans. Since the bill offers no guidance as to the function of the state bank, whether it is to accept deposits or make loans, or both, it is difficult to assess the risks of the state bank.

Is It Needed?

There are eight Hawaii banks headquartered in Hawaii. There is no evidence that the Hawaii banks are unable to meet the depository or credit needs of our businesses and residents. In addition, there are already state agencies which do engage in lending activities to meet certain community needs.

Capital Costs

The capital necessary for a state bank to be adequately capitalized under the FDIC regulations will depend on the risk-weighted assets of the state bank which will depend on its lending activity. The Federal Reserve Bank of Boston (issued in 2011) analyzed the costs of organizing a state bank in Massachusetts and concluded that the required capitalization of \$3.6 billion which was equal to 21% of the state direct debt. Obviously, the capital required in Hawaii would be smaller but at the same time, no doubt the burden on the state finances would be large.

Startup Costs

The startup costs are likely to be significant especially if the state bank will engage in deposits and checks. The infrastructure and cybersecurity costs will be significant, as well compliance with a myriad of banking regulations.

The bill provides for a withdrawal of state funds from banks. The Federal Reserve of Boston opined that if the state sought to withdraw funds from private depositories, it would be disruptive and would lead to a negative impact on the Massachusetts economy. Also, by impacting the Hawaii banks, there would be an adverse impact on Hawaii tax revenue as the franchise tax paid would be based on a lower revenue base.

This will also lead to a diminution of interest received by the state. Currently, the state funds are deposited to the winner of a public auction based on the interest rate the bank is willing to pay. Also, the state is protected from risk because the deposit is collateralized so the state does not have to rely on the limitations of FDIC deposit insurance (if it is even available).

If the state bank is going to engage in depository activity or making payment to employees, then there may be a question whether it is eligible to use the Federal Reserve payment system or FedNow (a proposed Federal Reserve payment system in the planning stages) and will then have to rely on a limited private payment system.

The foregoing should be considered a part of the startup costs.

Bond Rating Impact

If the state is to rely on bonds as a source of funds, the state must assess the risk of a lowering of the bond rating.

Using State Funds

If the state bank will rely on state funds as a source of funds, that means other uses of state funds such as for operating expenses, payroll, rainy day fund, and other human services needs, will have to rely on a lower set of funds for their needs.

Risk to State Funds

Hawaii banks are examined by both the federal and state examiners (unless you are a nationally chartered which banks are examined by federal examiners) to determine if the bank is compliant with regulations and especially, if there is a safety and soundness issue which endangers the financial soundness of the bank.

The state bank and Hawaii will not enjoy the benefit of federal and state examiners assessing the state bank.

Conclusion and Other Alternatives

It is crystal clear that a study is not needed because all other studies have shown the imprudence of a state bank. If the need is for credit, there are other alternatives within the state including through the Hawaii Finance and Development Corporation. The state can use existing loan programs and government agencies as a faster and more effective way to meet gaps in capital markets than establishing an entirely new organization.

Thank you for the opportunity to submit this testimony in opposition to HB 2628. Please let us know if we can provide further information.

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