

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

**Report to the Legislature on Act 32,
First Special Session Laws of Hawaii 2009
Relating to Mortgage Loan Originators**

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Section 10 of Act 32, First Special Session Laws of Hawaii 2009 (1st SSLH 2009) (SB1218, SD2, HD2, CD1) (“Act 32” or the “Act”), requires the Commissioner of Financial Institutions to prepare a report detailing the implementation of the Act. The report should include, but not be limited to:

- 1) an evaluation of administrative rules necessary for the implementation of this Act;
- 2) budget recommendations;
- 3) requests for staff and resources;
- 4) developments in federal law and regulations that affect the implementation of this Act;
- 5) guidance or recommendations put forth by the United States Department of Housing and Urban Development; and
- 6) findings, recommendations, and any proposed amendments or additions to the Act.

Background

The stated purpose of Act 32 is to implement a regulatory system, to be effective July 1, 2010, for the licensing and supervision of Mortgage Loan Originators (“MLOs”) – currently known as Mortgage Brokers or Mortgage Solicitors. Act 32 was adopted, following Congress’s passage of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (the “S.A.F.E. Act”).

The S.A.F.E. Act provides that states that do not implement a S.A.F.E. Act compliant regulatory system for MLOs will be subject to federal oversight and regulation of their residential mortgage industries. The Legislature concluded that it was in the best interests of the State and its residents for regulation of MLOs to remain the responsibility of the State and, as a result, adopted Act 32. The United States Department of Housing and Urban Development (“HUD”) has yet to confirm Act 32’s S.A.F.E. Act compliance.¹

¹ The Conference of State Bank Supervisors (“CSBS”), however, has advised that § -2(5) of the Safe and Fair Enforcement for Mortgage Licensing Act, set out in section 2 of Act 32, which exempts loan processors and underwriters from licensing conflicts

The authors of Act 32 recognized the novelty of the Act's regulatory scheme, and the challenges associated with its implementation. As a result, Act 32 provides for a one-year transition period during which chapter 454, Hawai'i Revised Statutes, continues to prescribe licensing and oversight of MLOs, while the Division of Financial Institutions ("DFI") enacts rules and procedures to fully implement the Act's regulatory system.

Considerations

The Act's stated intent is consistent with DFI's long-standing advocacy in favor of enhanced regulation and supervision of the Mortgage Brokerage industry. The activities of reputable Mortgage Brokers have a direct, valuable, immediate, and positive impact on Hawai'i's consumers and economy.

The Act has a number of provisions that make its implementation challenging.² Among the most significant challenges are funding and staffing for the program, which, it was understood from the beginning, would make compliance with the S.A.F.E. Act and Act 32 deadlines improbable. These concerns have only been exacerbated by the State's continued deteriorating financial condition.

While successful implementation of Act 32 remains a challenge, and for its success will likely depend on amendments to various S.A.F.E. Act deadlines and Act 32 itself, DFI immediately initiated contact with industry representatives upon the Act's passage and devoted resources to developing needed rules and statutory amendments.

The following are key considerations for the successful implementation of the Act:

- **Industry Participation**

DFI immediately enlisted the assistance of the Hawaii Association of Mortgage Brokers ("HAMB") and other Hawaii-licensed Mortgage Brokers and Solicitors in an effort to comply with the Act's deadlines. Discussions with Mortgage Brokers began in mid-July, and have continued to the present. Meetings focused on the need to prepare administrative rules, the administrative tasks related to the application process, background checks, pre-licensing testing, continuing education and the establishment and maintenance of an ongoing interface with the Nationwide Mortgage Licensing System ("NMLS"), which is the data base "backbone" of a S.A.F.E. Act compliant MLO program, and draft legislation to address amendments necessary to Act 32.

with the S.A.F.E. Act and must be amended to make it S.A.F.E. Act compliant. HUD has evidenced a strong interest in assisting states to ensure that plans are S.A.F.E. Act compliant rather than rejecting state plans.

² The State's plan must also be approved by the federal Department of Housing and Urban Development ("HUD"), which has evidenced a strong interest in assisting states to ensure that plans are S.A.F.E. Act compliant rather than rejecting state plans, as the alternative, in that event, would be the assumption by HUD of the regulatory responsibility.

- DFI Staffing and Funding

The Act provides no staffing and an insufficient amount of funding for DFI to perform the regulatory function during the transition year. Half of the total money appropriated in the first year is expected to be used to purchase Hawai'i's membership in the NMLS, with the bulk of the remainder going to pay for a temporary employee devoting the bulk of her time to the transition project. In addition, DFI has devoted significant administrative and overhead time to the Act 32 project. Budgetary principles prohibit DFI from spending additional amounts on the program in light of the appropriation included in the Act. Legislation is being drafted to address the staffing and budget issues.

- S.A.F.E. Act Preconditions

As a pre-condition to being S.A.F.E. Act compliant, the State must become a member of the NMLS, and DFI anticipates purchasing Hawai'i's NMLS membership with the moneys appropriated in Act 32. Since July 2009 DFI has participated in weekly NMLS "regulators only" conference calls that address system-related issues such as background checks, pre-licensing education and testing, and regulatory agency interaction, but the shortfall in program staffing and funding makes meaningful participation difficult.

- Operational/Timeline Issues

Hawai'i is not the only state whose S.A.F.E. Act program is being developed with very limited resources. DFI continues to explore, with other similarly-affected states, HUD, and NMLS, how states can comply in the face of fiscal challenges. As it stands, the next open date to join NMLS is October 2010, which, although beyond Act 32's effective date, should permit licensure to begin by January 1, 2011, consistent with revised deadlines (copy attached) expected to be included among the proposed amendments currently being drafted.

- Coordination with HUD and Anticipated S.A.F.E. Act Amendments

HUD officials are aware that Hawai'i is not the only State with S.A.F.E. Act implementation challenges, and they have made it clear that we should continue with our good faith efforts to become fully compliant.

Report Requirements

The information required for this report includes:

- An Evaluation of Administrative Rules Necessary for the Implementation of the Act

DFI and HAMB have completed draft rules to address Act 32 and various anticipated technical amendments. Upon adoption of any 2010 Act 32-related legislation, the rules will be completed, with anticipated final approval in November 2010.

- Budget Recommendations

The budget for Act 32 is primarily a function of, first, the fixed costs associated with S.A.F.E. Act compliance and, second, the number of existing Mortgage Brokers and Solicitors who choose to undergo the background checks, participate in the pre-licensing education and testing, and pay the fees associated with the new MLO program. Initial estimates have ranged from 3,000 to 1,500. The planning budget adopted by DFI to design and staff the program uses 2,000 MLOs as the initial number of participants, although the number of MLOs may decline in the face of increased fees, a continued slow down in real estate sales, and a real estate mortgage lending market that may be moving toward a more controlled "lender as broker" model.

The following chart provides budget estimates for a 2,000 member industry-funded MLO program.

MORTGAGE LOAN ORIGINATOR PROGRAM PROPOSED CASH FLOW BUDGET FY 10-14					
	<u>FY 10</u>	<u>FY 11</u>	<u>FY 12</u>	<u>FY 13</u>	<u>FY 14</u>
TOTAL REVENUES	\$ 250,000	\$ 1,507,000	\$ 1,002,800	\$ 940,260	\$ 782,135
TOTAL DIRECT COSTS	<u>315,266</u>	<u>871,702</u>	<u>730,282</u>	<u>641,755</u>	<u>555,748</u>
DIRECT CASH FLOW	(\$ 65,266)	\$ 635,298	\$ 272,518	\$ 298,505	\$ 226,387
TOTAL INDIRECT COSTS	<u>252,332</u>	<u>336,443</u>	<u>336,443</u>	<u>285,977</u>	<u>252,332</u>
TOTAL CASH FLOWS	(\$317,598)	\$ 298,855	(\$ 63,925)	\$ 12,528	(\$ 25,945)

▪ Requests for Staff and Resources

The following additional staff is required to implement and operate the Act 32 MLO program:

Supervisor – MLO Program –	1
Examiner III – Examination Branch –	1
Examiner II – Examination Branch –	2
Examiner III – Licensing Branch –	1
Examiner II – Licensing Branch –	2
Office Assistant III –	<u>1</u>
Total	8

Two of these staff (2 Examiner IIs) are intended to be temporary, and are not expected to be necessary after FY13. DFI's staffing projections were compared with other states that have already implemented S.A.F.E. Act compliant NMLS MLO programs and the foregoing plan is consistent with their experiences. Should the number of individuals applying for licenses under the new MLO program not meet projected levels, staffing can be scaled back to meet actual licensee levels.

▪ Developments in Federal Law and Regulations That Affect The Implementation of This Act

No recent developments, however federal agencies are expected to soon issue their own S.A.F.E. Act related rules and procedures governing depository institution MLO programs which will serve as precedents for the HUD rules applicable to state MLO programs.

▪ Guidance or Recommendations Put Forth by the United States Department of Housing and Urban Development

Contact with HUD was maintained throughout the 2009 Legislative Session and has continued during the Act's implementation period. Discussions with HUD staff, DFI and DFI's Deputy Attorney General have yielded the following "indications":

- States can establish "good faith" credentials by enacting a S.A.F.E. Act compliant bill on or before July 31, 2009. HUD's files show that Hawai'i has enacted a bill.

- HUD intends to review existing state statutes, identify any problems, and work with the states to achieve a compliant statute.
 - S.A.F.E. Act deadlines are, in fact, the deadlines; however, HUD will work with states demonstrating good faith and “best efforts.”
 - HUD prefers to bring the states into compliance, but reiterated its availability to establish its own program if states proved unable; HUD, however, currently has no plans in place to do this. It is the opinion of the Conference of State Bank Supervisors (“CSBS”), the key sponsor of the NMLS, that HUD has no wish to implement and administer state MLO programs.
- Findings, recommendations, and any proposed amendments or additions to the Act

DFI has been working closely with HAMB and other Hawaii Mortgage Brokers and Solicitors to identify technical and operational issues that need to be addressed in an amended Act. At this point, we expect that the industry will be proposing and supporting amendments that are likely to include:

1. DFI staffing to adequately administer the State S.A.F.E. Act compliant MLO program.
2. Funding to cover program expenses until licensing fee related cash flows commence in November/December 2010.
3. Addition of Mortgage Broker companies as licensees under Act 32, which will provide framework for individual MLO affiliation and licensing.
4. Deletion of exemption for independent contractor underwriters and loan processors.
5. Extension of Chapter 454 HRS to provide continued licensing of Hawaii Mortgage Brokers and Solicitors until Act 32 licensing becomes effective on January 1, 2011.
6. Increases in fees for licensing and program administration.

Conclusion

Act 32 will require amendment and federal agency support even to meet the belated achievement of its goal. Nevertheless, with the demonstrated interest of the

Legislature, and in view of the cooperation and the attention shown by the affected industry during this off-session, that appears now to be possible.

DFI, assisted by Hawaii mortgage broker industry participants, the NMLS transition staff, and CSBS has made significant progress since enactment. We anticipate, with the introduction of adequate funding and staffing to be approved in the 2010 Legislative Session, providing a fully functioning, S.A.F.E. Act compliant program accepting applications from State MLO applicants by November 2010 for licenses to be issued in January 2011.

Mortgage Loan Originators Act 32 (MLOA) - REVISED December 3, 2009
Timeline for Implementation

	07/2009	08/2009	09/2009	10/2009	11/2009	12/2009	FY 10					FY 11					10/2011
1 Governor's Veto Overridden																	
2 DFI commences ongoing dialogue with HAMB on Act 32 Implementation																	
3 Work w/ HAMB to Draft and Adopt Administrative Rules																	
4 DFI receives \$150,400 to partially defray implementation costs of MLOA																	
5 Act 32 amended																	
6 Appropriation of \$xxx,xxx made to cover initial program funding requirements																	
7 Legislative Authorization to Hire Approved																	
Hire Manager																	
8 Hire 1 Office Assistant																	
9 Hire 3 Licensing Examiners																	
10 Hire 2 Field Examiners																	
11 Commissioner Issues Orders to Implement Provisions of Act 32 (Amended in 2010)																	
12 Undergo National Mortgage Licensing System (NMLS) Training																	
13 Establish pre-licensing education and examination																	
14 Set up application/notification forms and procedures																	
15 Set up criminal history record check forms and procedures																	
16 Go live on NMLS																	
17 STATUTORY DEADLINE PVL courses issued or renewal of licensees under HRS 454																	
18 STATUTORY DEADLINE DFI commences licensing new applicants																	
19 Develop Field Examination Program																	
20 Hire 1 additional Field Examiner																	
21 DFI commences licensing applicants in accordance with Act 32 /SAFE Act																	
22 Establish continuing education programs																	
23 Program is up and running. Chapter 454, HRS is repealed																	