



**TIER 1 INFORMATION
SEPTEMBER 2004**

AGENCY INFORMATION

Agency Name: Department of Financial Institutions (DFI)

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AGENCY RESPONSIBILITIES

The Department of Financial Institution's mission is to regulate our state's financial services industry to protect the public, promote economic vitality, and preserve integrity in the marketplace. In fulfilling its mission, the Department conducts four core programmatic activities:

Chartering, Licensing and Registration

The Department of Financial Institutions evaluates and approves new applications, mergers, conversions, branches, and corporate governance changes for banks and credit unions. The Department also conducts licensing, registration and exemption activities for the following financial entities and persons: broker dealers, broker dealer representatives, investment advisers, investment adviser representatives, securities issuers, franchises, franchise brokers, business opportunities, escrow agents, escrow officers, mortgage brokers, check cashers and sellers (payday lenders), money transmitters, currency exchangers, and consumer loan companies.

Examinations

The Department performs several types of examinations. The three primary examinations are: (1) Compliance and for cause examinations of securities broker dealers, mortgage brokers, mortgage broker-dealers, investment advisers, escrow agents, escrow officers, debenture companies, check cashers and sellers (payday lenders), consumer loan companies, money transmitters, and currency exchangers; (2) safety and soundness examinations of banks, credit unions, debenture companies, money transmitters, trust companies, Small Business Association (SBA) lenders, and industrial development corporations; and (3) information system examinations of banks and credit unions.

Enforcement

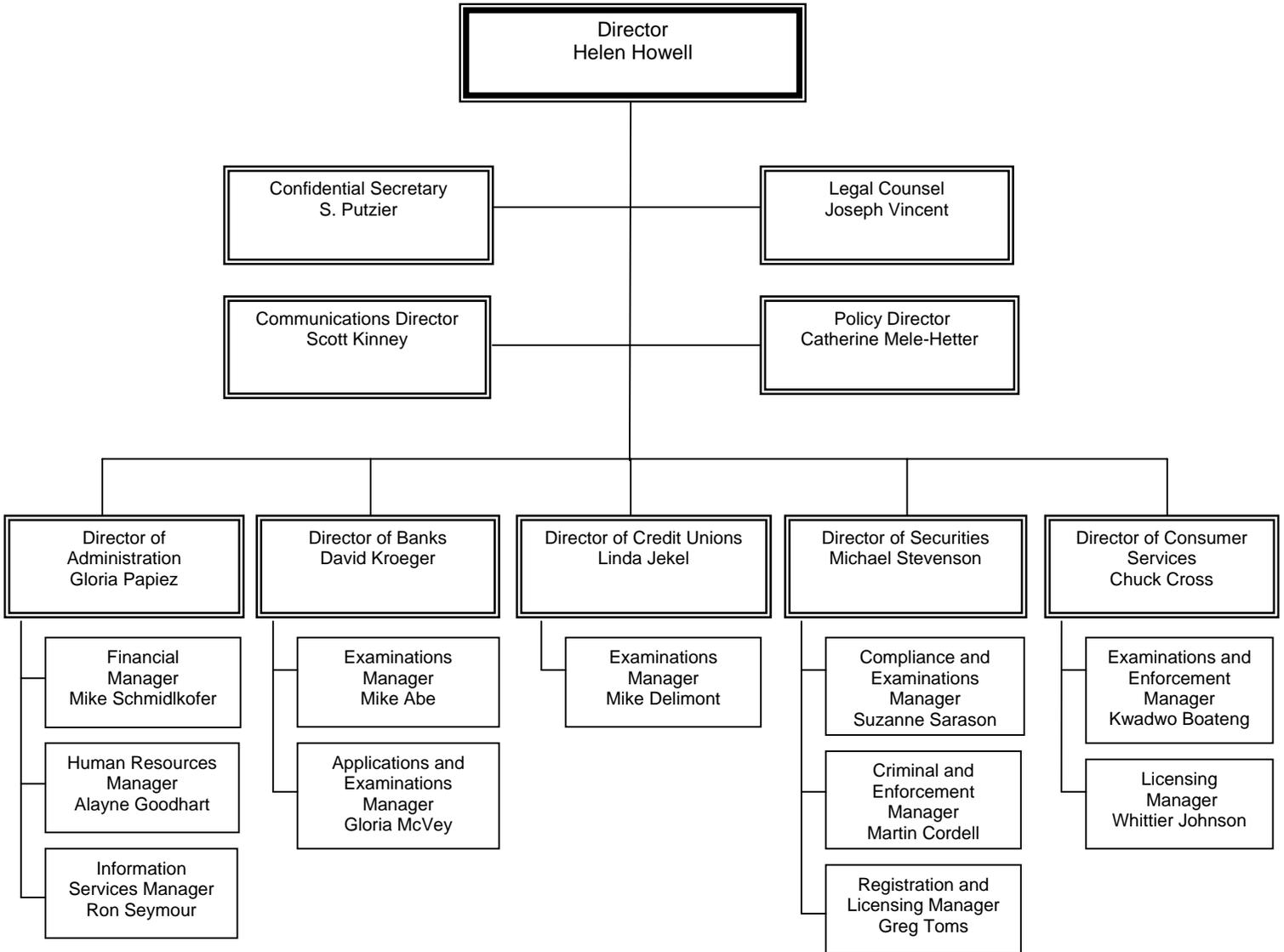
The Department conducts various types of supervisory, surveillance and enforcement activities to detect and take corrective action for violations of the regulatory and anti-fraud statutes applicable to financial institutions. Activities include: complaint processing, investigation, and appropriate action against securities issuers and brokers, investment advisers, mortgage brokers, check cashers and sellers (payday lenders), money transmitters, currency exchangers, consumer loan companies and escrow agents; and investigation and appropriate actions against banks and credit unions. Coordination and assistance to other law enforcement agencies and prosecutors, and providing testimony in courts of law are additional activities associated with enforcement.

Education and Public Outreach

The Department conducts consumer education and stakeholder outreach activities, and provides technical assistance and regulatory guidance to banks, credit unions, securities and consumer lending industry participants. Activities include: presentations, town meetings, press conferences, technical assistance, advisory letters and bulletins, and other related activities that provide education and information to assist consumers and other stakeholders.

DEPARTMENT OF FINANCIAL INSTITUTIONS

August 25, 2004



Department of Financial Institutions

2003-2005 Biennium
(Budget Period-Two Fiscal Years)

Allotted Revenue Estimates

<i>By Revenue Source</i>	<i>Amount</i>
Banking Licenses and Fees	\$15,246,149
Credit Unions Licenses and Fees	4,323,490
Franchise Licenses	511,943
Less transfer to the General Fund	-445,390
Securities Licenses and Fees	63,822,348
Less transfer to the General Fund	-55,525,443
Fines and Forfeits	200,000
Total-Source	\$28,133,097

<i>By Fund</i>	<i>Amount</i>
Securities Prosecution Fund	\$200,000
Mortgage Lending Fraud Prosecution Fund	1,234,992
Financial Service Regulation Fund	26,698,105
Total-Fund Summary	\$28,133,097

Allotted Program Expenditure

<i>By Program</i>	<i>FTE's</i>	<i>Amount</i>
Administration	24.1	\$5,048,793
Division of Banks	29.7	5,945,661
Division of Credit Unions	16.7	3,786,623
Division of Securities	49.1	9,024,139
Division of Consumer Services	27.9	6,228,374
Total-Programs	147.5	\$30,033,590

<i>By Fund</i>	<i>Amount</i>
Securities Prosecution Fund	\$161,000
Mortgage Lending Fraud Prosecution Fund	1,185,000
Financial Service Regulation Fund	28,687,590
	\$30,033,590

Projected Ending Fund Balance at 6/30/05

<i>Fund</i>	<i>Amount</i>
Securities Prosecution Fund	\$350,000
Mortgage Lending Fraud Prosecution Fund	\$279,992
Financial Service Regulation Fund	\$7,265,020

¹ Agency's working capital reserve \$4,025,006

DFI MAJOR ISSUES

1. CHANGING REGULATORY ENVIRONMENT

Issue:

- Expanding technology is rapidly changing the way the financial services sector structures, delivers, and services its products.
- New products and services such as stored value cards, refund anticipation loans and on-line trading are being marketed before consumer protections are enacted.
- Lines are blurring between financial service providers such as Wal-Mart check cashing, Costco VISA credit cards, and State Farm mortgages.

Urgency:

Regulators are challenged to keep pace with financial service providers that are experiencing phenomenal growth, inventing new products/services, becoming more sophisticated in technology, and crossing into other industries.

Significance:

- A major regulatory concern is to ensure that regulated entities are equipped to secure and manage new technological solutions while at the same time ensuring that the regulatory structure does not inhibit change that is in the consumers' best interest.
- Consumer protection laws need to be expanded to cover new financial service products. However, state consumer protection laws in other states have been preempted by federal agencies. (See page 2, *Federal Preemption Of State Laws*)
- Regulators of different industries (such as banking, securities, and insurance) will be working together to ensure regulated entities that cross into other industries comply with applicable laws.

Key Players:

- Federal regulators and national associations of regulators: Federal Deposit Insurance Corporation, Board of Governors of the Federal Reserve System, Federal Financial Institution Examination Council, National Credit Union Administration, American Association of Residential Mortgage Regulators, National Association of Consumer Credit Administrators, Money Transmitter Regulators Association, and North American Securities Administrators Association.
- Office of the Attorney General, Office of the Insurance Commissioner, and other state regulators of financial service providers.

Status:

DFI continues to leverage its examination and enforcement role through partnerships with others and the use of technology. In addition, DFI has submitted significant decision packages to increase the number of examiners and enhance examination technology.

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DFI MAJOR ISSUES

2. FEDERAL PREEMPTION OF STATE LAWS

Issue:

The Office of Comptroller of Currency (OCC) recently ignored the consistent intent of Congress and U.S. Supreme Court decisions and adopted OCC Rules that:

- Immunize national banks and their mortgage company operating subsidiaries from basic and fundamental Washington state laws that regulate real estate lending.
- Prevent the DFI from examining or investigating mortgage company subsidiaries of national banks that are subject to state consumer protection and licensing laws.
- Prevent the Attorney General from enforcing the Washington Consumer Protection Act against mortgage company subsidiaries of national banks.

Urgency:

At stake is the sovereignty of every state to regulate those entities that it charters and incorporates. The states need to persuade Congress to rescind the OCC Rules. Key federal appeals by Connecticut and Michigan may take several more years with no predictable guarantee of a result in favor of the states. If Congress cannot be persuaded to do so, the states must then grapple with an industry-sponsored proposal for national consumer protection standards against **predatory lending** that claims to offer nationwide uniformity and predictability for the financial services industry. In that event, the states should consider a compromise with the industry, provided that (1) mortgage company operating subsidiaries of national banks are still subject to charter or license by the states and (2) the states retain a significant regulatory role by being able to enforce the national consumer protection standards at a state level.

Significance:

Left unchecked, the OCC Rules would be irreversibly damaging. Consumer protection in Washington State will suffer. Banks regulated by the DFI, which now operate in multiple states, may be persuaded by the OCC to switch to a national charter to avoid state regulation. The viability of the state banking charter and the dual banking system may be undermined. Business competition and the historical innovation provided by state banks will be stifled.

Key Players:

Opponents of using the OCC Rules include the Conference of State Bank Supervisors (CSBS), National Governors Association (NGA), National Conference of State Legislatures (NCSL), National Association of Attorneys General (NAAG), and the National Association of Realtors®.

Status:

DFI will continue to monitor this issue and its impact on all industries the DFI regulates. If presented with the proper case and with the advice of the Attorney General, DFI may — like Connecticut and Michigan — “test” the OCC Rules in court.

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DFI MAJOR ISSUES

3. TRANSPARENCY AND EFFECTIVE CONSUMER PROTECTION IN THE PAYDAY LENDING INDUSTRY

Issue:

Payday lenders make short term, high cost loans to consumers. Currently the DFI has insufficient information concerning the market and business practices of payday lenders.

- National reports, recent complaints, news stories and other anecdotal information strongly indicate that this industry should have greater regulatory oversight and consumer protection. However, regulators in our state and across the country have found it difficult to make the industry's business practices "transparent."
- This lack of "transparency" is attributable to a still-young industry (approximately 10 years old) that is not regulated in all states. In states where payday lending is regulated, such as Washington, the governing laws and regulations are relatively new. This highly profitable industry has been critical of regulatory efforts to increase "transparency" claiming the cost of consumer protection compliance programs will impact its "bottom line."

Urgency:

Increased sophistication in the delivery of existing services, plus the emergence of new services enabled by information technology (IT), holds the potential to greatly impact consumers. The payday lending industry is pioneering new products and business practices at a speed that has severely outpaced the ability of regulators to understand how the core business of payday lending has evolved.

Significance:

- Dollars to consumers are real. Recent evidence shows that consumers may pay as much as \$2,000 or more per year for the ability to borrow \$500. Implications for low income, middle income and military personnel are significant.
- Not unlike other industries, payday lenders would prefer that government regulation remain static or even be curtailed. By contrast, respected consumer advocacy groups now plead for heightened consumer protection and regulatory "transparency." Additionally, several banks nationwide, attracted by the huge profits to be made from payday lending, are now endorsing and supporting storefront payday lenders by "renting" their charters to some payday lenders who wish to preempt state licensing laws.

Key Players:

Payday lenders, banks, credit unions, consumers and consumer advocates.

Status:

Regulators nationwide are beginning to establish a foothold in regulating this industry. Enforcement cases are being filed and better regulations written, but regulators are still far from gaining a clear picture of the industry and effective tools to protect consumers.

Web Links: www.dfi.wa.gov; www.nclc.org; www.predatorylending.org; www.cfsa.net; www.fisca.net.

Staff Contacts:

- Chuck Cross, Division Director, ccross@dfi.wa.gov, 360-902-8733.
- Catherine Mele-Hetter, Policy Director, cmele@dfi.wa.gov, 360-902-0515

DFI MAJOR ISSUES

4. CONSUMER EDUCATION

Issue:

Changes in our economy and job market have impacted the way consumers spend money, save money – even retire. However, consumers continue to spend more and save less.

- With the complexity of the various financial products now available in the marketplace, consumers are unknowingly entering into risky financial situations.
- Washington State cannot afford to invest all the enforcement resources necessary to eliminate the problem. Educating consumers before they enter into financial transactions is key to preventing financial fraud.

Urgency:

- Financial fraud continues to increase. In particular, the numbers of senior citizens, college students, Hispanics, Native Americans, and military personnel that become victims of financial fraud are increasing.

Significance:

- Over 12,000 Washington consumers came forward as victims of predatory lending practices during the largest mortgage fraud investigation and settlement in our nation's history (Household Finance).
- In a study commissioned by DFI measuring the financial literacy of Washington consumers and how best to reach them, consumers requested an objective or neutral resource to offer financial education. Although many financial institutions offer financial literacy programs, less than 1% of those surveyed used these resources.
- In a survey conducted by the American Association of Retired Persons (AARP), over 1.1 million residents in Washington feel that they have been victims of financial fraud in the past year. In most cases, the instances went unreported because the victims blamed themselves for being taken advantage of and were too embarrassed to contact officials.
- DFI continues to experience increases in consumer complaints and enforcement cases.
- Senior level representatives from all branches of the military based in Washington State have contacted DFI to request immediate assistance in educating enlistee's to the dangers of payday lending and investment scams.
- Financial skills must be taught early. Nationally, research has shown that only 10% of students report learning about managing money in school. The other 90% claim to have attempted to figure it out through trial and error. Children must receive basic economic literacy to take control over their financial lives, and their futures.

Key Players:

Consumers and consumer advocates, DFI communications and outreach team, and members of the legislature.

Web Links: www.dfi.wa.gov; www.atq.wa.gov; www.ftc.gov; www.aarp.org

Staff Contacts:

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DFI MAJOR ISSUES

5. PROPOSED NEW STATE SECURITIES ACT

Issue:

- The new Uniform Securities Act (USA) is a major piece of regulatory legislation affecting investors and businesses raising capital in the state of Washington.
- The USA is drafted and sponsored by the National Conference of Commissioners on Uniform State Laws and will be introduced by uniform law commissioner, Judge Marlin Appelwick, of the Washington State Court of Appeals.

Urgency:

The USA will be introduced in the 2005 session.

Significance:

- The USA repeals and replaces entirely the present uniform law, ch. 21.20 RCW, which has been in effect since 1959.
- The legislature will face many potential policy issues including:
 1. Setting registration and filing fees, which may impact DFI agency operations and revenue to the general fund;
 2. Balancing the scope of civil and criminal actions and the length of statutes of limitation, which affect the rights of plaintiffs and defendants;
 3. Determining the jurisdiction over insurance agents selling hybrid securities products, such as variable annuities and viatical settlements;
 4. Regulating banks and other financial institutions as securities broker-dealers; and
 5. Dealing with many other regulatory and consumer protection issues.

Key Players:

- Participants from financial and investment service groups may include: the American Bankers Association; American Bar Association; American Council of Life Insurers; Certified Financial Planners; Financial Planning Association; Investment Company Institute, Investment Counsel Association of America; National Association of Securities Dealers; New York Stock Exchange; North American Securities Administrators Association; Securities and Exchange Commission; and Securities Industry Association.
- Consumer Groups – American Association of Retired Persons; Consumer Federation of America; and National Consumer League

Status:

Passage of legislation is expected in the 2005 or 2006 legislative session.

Web Links: www.NCCUSL.org; <http://www.nasaa.org>

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